S. HRG. 98-1276

THE CONSUMERS' RAIL TRANSPORTATION ANTIMONOPOLY ACT

HEARING

BEFORE THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

NINETY-EIGHTH CONGRESS

SECOND SESSION

ON

S. 2417

A BILL TO AMEND THE SHERMAN ACT TO PROHIBIT A RAIL CARRIER FROM DENYING TO SHIPPERS OF CERTAIN COMMODITIES, WITH INTENT TO MONOPOLIZE, USE OF ITS TRACK WHICH AFFORDS THE SOLE ACCESS BY RAIL TO SUCH SHIPPERS TO REACH THE TRACK OF A COMPETING RAILROAD OR THE DESTINATION OF SHIPMENT

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THE CONSUMERS' RAIL TRANSPORTATION ANTIMONOPOLY ACT—S. 2417

TUESDAY, SEPTEMBER 18, 1984

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The committee met, pursuant to notice, at 2:10 p.m., in SD–226, Dirksen Senate Office Building, Hon. Alan Simpson (acting chairman) presiding.

Also present: Senators DeConcini, Baucus, and Biden.

Staff present: Boyd Hollingsworth, Karen Gordon, Cindy Lebow, Mary B. Troland, Bob Fiedler, and Matt McCoy.

OPENING STATEMENT OF SENATOR DENNIS DeCONCINI

Senator DECONCINI. Chairman Simpson is on his way, but has advised that he has no problem with commencing the hearings of the full Judiciary Committee. I want to thank Senator Simpson for taking the time and interest in having some hearings on S. 2417, and also Senator Thurmond and the ranking member, Joe Biden.

This bill has a varied following, as demonstrated by the parties represented here today that will come in and out during the committee hearing, I anticipate. In addition to affecting consumers, the legislation also affects areas of agriculture, industry, utilities, and others, all of which employ the railroad to ship the respective commodities.

There have been concerns raised that S. 2417 would return the railroad industry to the pre-Staggers Act period of regulation. This is not the case. S. 2417 is intended to address only one issue, and that is the captive shipper issue.

S. 2417 intends to promote competition by having market forces determine rail transportation rates rather than allowing the railway-controlling monopolies to fix the rate on that particular line.

We have before us today what can truly be called a bipartisan issue affecting all regions of the Nation. Because of the fast-approaching close of the 98th Congress, hearings on this issue will be limited during this session. Yet, with this broad interest displayed here today and the list of witnesses, I hope the committee could schedule further hearings early next year on S. 2417 or its equivalent, early in the 99th Congress.

Before we begin with the first witness, I wish to place S. 2417 in the record.

[Text of S. 2417 follows:]

II

98TH CONGRESS
2D SESSION

S. 2417

To amend the Sherman Act to prohibit a rail carrier from denying to shippers of certain commodities, with intent to monopolize, use of its track which affords the sole access by rail to such shippers to reach the track of a competing railroad or the destination of shipment.

IN THE SENATE OF THE UNITED STATES

MARCH 13 (legislative day, MARCH 12), 1984

Mr. DECONCINI (for himself and Mr. BAUCUS) introduced the following bill; which was read twice and referred to the Committee on the Judiciary

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A BILL

To amend the Sherman Act to prohibit a rail carrier from denying to shippers of certain commodities, with intent to monopolize, use of its track which affords the sole access by rail to such shippers to reach the track of a competing railroad or the destination of shipment.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Sherman Act is amended by inserting after section 8 the following new section:

"SEC. 9. (a)(1) It shall be unlawful for a rail carrier, with intent to monopolize, to deny to any shipper the use on reasonable terms of a railroad facility which is the sole facili-

ty over which such shipper can move its goods by rail to connect with the tracts of a competing rail carrier or to reach the destination of shipment.

"(2) The terms offered by the rail carrier for the use of such sole facility shall not be deemed reasonable if—

"(A) they condition the use of the sole facility upon use of other facilities of the rail carrier;

"(B) the rates required by the rail carrier for use of the sole facility are such as to yield a revenue-to-variable cost ratio higher than the lower of the revenue-to-variable cost ratios yielded by—

"(i) its single line rate or

"(ii) its division of a competing joint line rate; if there are such, to the destination of shipment; or

"(C) the rates required by the rail carrier for use of the sole facility are higher than would, under generally accepted regulatory standards, yield a fair return on the proportion of the rail carrier's prudent investment in the railroad facility that the shipper's traffic bears to all traffic using such railroad facility.

"(3) The shipper may elect to connect with water carriage at any point within or not substantially beyond the first rail connection with a competing rail carrier.

"(b) A rail carrier shall be conclusively presumed to have denied use of such railroad facility with intent to monopolize if it has denied use of the facility upon reasonable terms to a shipper and is not permitting any other rail carrier to use the railroad facility to transport the shipper's goods.

"(c) A shipper permitted to move goods over a railroad facility pursuant to the requirements of subsection (a) above shall not be deemed a 'rail carrier' or a 'carrier' under any provision of law.

"(d) For purposes of this section—

"(1) the term 'rail carrier' means any 'rail carrier' as defined in section 10102(19) of title 49, United States Code, subject to the jurisdiction of the Interstate Commerce Commission under title 49, United States Code, chapter 105, subchapter I;

"(2) the term 'shipper' includes, but is not limited to, a person engaged in a business other than transportation who, in furtherance of such business, moves its own goods;

"(3) the term 'railroad facility' includes all railroad components enumerated in section 10102(20) (A), (B), and (C) of title 49, United States Code;

"(4) the phrase 'use of a railroad facility' means the movement of any shipper's goods consisting of coal, ore, grain, forest products, chemicals, or fertilizers, and

includes movement of such shipment over such railroad facility either by shipper with its own rolling stock or by the rail carrier;

"(5) the phrase 'permitting any other rail carrier to use the railroad facility' means permitting such other carriers to use such railroad facility from the point of origin of the shipment to the connecting point with the track of the competing carrier;

"(6) the term 'track of the competing carrier' means track subject to the competing carrier's use but does not include tracks jointly used with the rail carrier denying use of the sole facility.

"(7) the term 'rail carrier' includes all affiliates of the rail carrier controlled by it or under common control with it.

Senator DECONCINI. Our first panel will be a panel of three: Ira McKeever, president of Western Coal Development, W.R. Grace & Co.; Prof. Scott Atkinson, University of Wyoming; and Dr. Stephen Anderson, director of research, Consumer Energy Council of America.

Gentlemen, if you would come and sit at the head table here, I would ask that your full statements be printed in the record. We do have a host of witnesses today and we will limit the actual testimony of each of you to the 5-minute rule. When the red light goes on, we would ask that you terminate your remarks at that time.

Do you have an order that you care to go in? If not, I will start with Mr. McKeever, unless someone else has a different plan among those of you there.

Mr. McKeever.

STATEMENT OF A PANEL CONSISTING OF: IRA E. McKEEVER, JR., PRESIDENT, WESTERN COAL DEVELOPMENT, W.R. GRACE & CO., WASHINGTON, DC, ACCOMPANIED BY JOHN N. THURMAN, GROUP VICE PRESIDENT, W.R. GRACE & CO., AND DONALD CRANE, CONSULTANT; SCOTT ATKINSON, PROFESSOR, UNIVERSITY OF WYOMING, LARAMIE, WY.; AND DR. STEPHEN O. ANDERSEN, DIRECTOR OF RESEARCH, CONSUMER ENERGY COUNCIL OF AMERICA, WASHINGTON, DC

Mr. McKEEVER. Thank you, Mr. Chairman. I have with me our group vice president, John Thurman, on my left here, and our consultant, Don Crane.

My name is Ira McKeever, president of the Western Coal Development for W.R. Grace. We are partners with the Hanna Mining Co. of Cleveland, OH, in the Colowyo mine and the Hayden Gulch mine, along with three other properties in northwest Colorado.

The combined capacity of these five properties, if fully developed, would be in excess of 8 million tons a year, more than double our current production level of 3.5 million tons.

The reason we have not further developed these mines is that we have been unable to obtain long-term contracts since 1980. We have also been advised by another of our long-term buyers, Central Power & Light Co. of Corpus Christi, TX, that they will phase out their purchases of Colowyo coal by the end of 1994.

The principal reason we have not been able to negotiate any new long-term contracts or expand existing long-term contracts is the rapid increase in freight rates experienced by our customers as a result of the monopoly position of the Denver & Rio Grande Railroad. All coal produced by our two operating mines or to be produced by the other three properties is captive.

With respect to Central Power & Light, the original rate quoted in 1977 was $13 a ton from Colowyo to the Coleto Creek station. When shipments started at the end of 1979, the rate imposed by the Denver & Rio Grande was $20.85 a ton, a 60-percent increase in 2 years.

Even before the Staggers Act, the monopoly position of the Denver & Rio Grande Railroad allowed them to take unfair advantage of its captive shippers. In a local context, shipments of coal from Colowyo to a utility about 31 miles by rail incur a cost of 11 cents a ton-mile versus an independent estimate of 4.5 cents a ton-mile over track that is, for the most part, owned and maintained by Colowyo.

The Staggers Act of 1980 has made matters worse because it effectively deregulated the railroads without adequately dealing with the monopoly issue. Most current efforts at redressing this situation are aimed at changing the regulatory rules for captive shippers.

While this is a worthwhile effort, it does not address the basic problem, which is the monopoly position of the railroads. One way to break the railroad monopoly would be to legislate trackage rights. Trackage rights now exist between many railroads, under which the railroads are allowed to use the tracks of other railroads in exchange for adequate compensation.

If this limited concept of trackage rights were extended to include captive shipments, there would be no monopoly. Any railroad anywhere in the country could compete for Colowyo coal shipments. With competition, there would be no need for regulation of freight rates.

Under the trackage rights proposal, fair rates for the use of the tracks would be self-enforcing and not require a regulatory bureaucracy for attainment. If a carrier set an unduly high rate for the use of its tracks, the proposal at hand places the presumptive burden on that carrier to prove in court that the rate is just and nonprohibitive.

We anticipate that such a challenge would be brought by another carrier having reliable and credible data of its own on what would constitute a reasonable rate for the use of the tracks.

Grace does not see this proposal as weakening the control any railroad has over its tracks. This proposal does not challenge or change the attributes of ownership. This proposal does not result in encouraging unsafe operating conditions or overloading the rail system.

What the proposal does accomplish is that such ownership cannot be used in a monopolistic way with respect to pricing and access to tracks.

In summary, Grace believes that Congress require trackage rights be offered in all situations involving captive shippers of bulk commodities such as coal and this is the most appropriate approach to correcting the present monopoly problem.

This approach is good public policy for the following reasons: One, it is a fair and understandable concept; two, it corrects the root problem of monopolistic management; three, it is self-enforcing; four, the consumer benefits from allowing competition to set the lowest freight rate; five, it increases the rationale for State public utility regulatory commissions to accept the costs of delivered fuel in electric rate proceedings, and, six, it does not amend the Staggers Act.

The bill being considered by your committee, S. 2417, would be one way of achieving trackage rights and doing away with the present monopoly structure. Grace looks forward to working with the committee. We urge the committee to consider S. 2417 favorably.

Thank you.

[The prepared statement follows:]

PREPARED STATEMENT OF IRA E. McKEEVER, JR.,
PRESIDENT, WESTERN COAL DEVELOPMENT,
W. R. GRACE & COMPANY

IN SUPPORT OF S. 2417

I am Ira McKeever, President of W. R. Grace & Co.'s Western Coal Development.

We are partners with the Hanna Mining Co. of Cleveland, Ohio, in the Colowyo Mine and the Hayden Gulch Mine, both in Northwest Colorado.

The Colowyo Coal Mine is the largest coal mine in Colorado, producing over three million tons of coal per year and employing over 400 people. The total investment in the mine exceeds $100 million. The Hayden Gulch Mine is producing about a half million tons per year. In addition to these two operating mines, we own federal, state and private coal leases at three other sites in Northwest Colorado (Hayden Gulch West, Little Bear Creek and Chokecherry). The combined capacity of these five properties, if fully developed, would be in excess of 8 million tons per year, more than double our current production level of 3.5 million tons.

The reason we have not further developed these properties is that we have been unable to obtain any long-term contracts since 1980. In fact, we have recently found it necessary to renegotiate one of our existing contracts (with Celanese Chemical Corp.), which will result in closing down the Hayden Gulch Mine at the end of 1986, putting 60 people out of work. We have also been advised by another of our long-term buyers, Central Power & Light Co. of Corpus Christi, Texas, that they do not intend to exercise their option to purchase additional coal, beginning in 1990, and will phase out their purchases of Colowyo coal by the end of 1994.

The principal reason we have not been able to negotiate any new long-term contract since 1980, and the reason we are losing existing long-term contracts with Celanese and Central Power & Light is the rapid increase in freight rates experienced by our customers as a result of the monopoly position of the D&RGW Rail-

road. All coal produced by our two operating mines or to be produced from the other three properties, is captive to the D&RGW Railroad.

Inordinately high freight rates also prevent us from supplying additional coal, on an annual basis, to Central Power and Light. Earlier this year, coal from the Colowyo Mine delivered to CP&L was ranked 14th on competitive bid list even though we were informed on the basis of the f.o.b. price of the coal and quality, our bid was ranked first.

With respect to CP&L, the original rate quoted in 1977, was $13.00/ton from Colowyo to the Coleto Creek station. When shipments started at the end of 1979, the rate imposed by D&RGW was $20.85/ton - a 60% increase in two years. The rate is now $29.93/ton, an increase of 130% over the quoted amount at the time of contract. Even before the Staggers Act, the monopoly position of the D&RGW railroad allowed them to take unfair advantage of its captive shipments. This situation has been exacerbated since the deregulation of the railroads.

Similarly, shipments to the Celanese plant in Pampa, Texas, cost $11.14/ton in 1980. It is now $16.51/ton, an increase of 48%.

In a local context, shipments of coal from Colowyo to a utility about 23 miles distant incur a cost of 11 cents/ton mile (vs. an independent estimate of 4.5 cents/ton mile) over track that is for the most part owned and maintained by Colowyo. We estimate this rate to be approximately 400% over the direct costs to D&RGW in the provision of locomotives and crew and yield well over 100% return annually to the D&RGW on their investment allocated to the operation. (See attachment A for details on these examples.)

We are not alone, of course. Most western coal shippers, as well as shippers of other bulk commodities such as grain and ore, are in essentially the same position.

For instance, in 1983, 13 million tons of coal were produced in Colorado for markets other than mine-mouth power generation. Of this amount, 97% is captive to the D&RGW railroad. Similarly, all of the producing coal mines in Utah are captive to the D&RGW

unless they utilize truck haulage for deliveries from the mine to the mine-mouth power plants. (See Attachment B and C for maps of Western Colorado and Utah showing rail lines and locations of coal mines.)

The Staggers Act of 1980 has made matters worse, because it effectively deregulated the railroads, without adequately dealing with the monopoly issue. Most current efforts at redressing this situation are aimed at changing the regulatory rules for captive shippers. While this is a worthwhile effort, it does not address the basic problem, which is the monopoly position of the railroads. As long as the monopoly position is allowed to continue, shippers will always be fighting an uphill battle to receive fair freight rates and the consumer will have to pay for it.

We have seen dramatic results from deregulation of the airline industry. Low passenger fares have been achieved, not by improving the regulatory system but by removing it. Competition has driven fares down, and forced the airlines to reduce their cost structure to fit within the lower fare structure. This is, of course, the way most other American businesses operate: competition sets the price structure and the most efficient producers make the most profit within this price structure.

The difference between the airlines and the railroads is that airlines do not have a monopoly, but railroads do. Airlines do not own the airports, railroads do own the railroad tracks. If this monopoly could be broken, railroads would be able to compete with each other, and the market place would set freight rates just as it does in the airline business.

One way to break the railroad monopoly would be to legislate <u>trackage rights</u>. Trackage rights now exist between many railroads, either as a result of regulatory action or under agreements entered into between individual railroads, under which the railroads are allowed to use the tracks of other railroads in exchange for adequate compensation. If this limited concept of trackage rights were extended to include captive shipments, there would be no monopoly: any railroad, anywhere in the country, could compete for Colowyo coal shipments, just as any airline can compete freely

anywhere within the country. With competition, there would be no need for regulation of freight rates.

There would, of course, continue to be the need for regulation. However, this would focus on the safety of operations of the railroads, the licensing of engineers, etc. I believe these activities are already covered by the Department of Transportation.

However, under the trackage rights proposal, establishing fair rates for the use of the tracks would be self-enforcing and not require a regulatory bureaucracy for attainment. If a carrier set an unduly high rate for the use of its tracks, the proposal at hand places the presumptive burden on that carrier to prove in court that the rate is just and non-prohibitive. We anticipate that such a challenge would be brought by another carrier having reliable and credible data of its own on what would constitute a reasonable rate for use of tracks.

We see this proposal working quite easily. A utility or a shipper wanting coal delivered from point A to point B would contact several rail carriers and ask for quotes. Specifications with respect to the tonnage, rate of delivery, characteristics of the loading and unloading facilities, and so forth, would be provided. The competing rail carriers would assemble appropriate data, including the rate for trackage use from carriers currently having monopoly access to any portion of the route from origin to destination. Quotes would be submitted and differences would reflect the competitive efficiencies between the individual carriers rather than the condition of having sole access to particular stretches of track which are essential for the service.

Grace does not see this proposal as weakening the control any railroad has over its tracks. The railroad of ownership maintains its position of ownership, management, scheduling, signaling, ability to arrange trackage with other roads, maintenance and other aspects of operations. This proposal does not challenge or change these attributes of ownership.

This proposal does not result in encouraging unsafe operating conditions or overloading a rail system. For instance,

most likely the rail carrier of origin will be one of the carriers competing for the business and would be able to maintain the same scheduling and operational control over its own trains as well as those of another carrier if it were awarded the business. This type of scheduling and management control is common to all instances of trackage agreements now in existence.

What the proposal does accomplish is that such ownership cannot be used in a monopolisitic way with respect to pricing and access to the tracks.

In summary, Grace believes that Congress requiring trackage rights be offered in all situations involving captive shippers of bulk commodities, such as coal, is the most appropriate approach to correcting the present monopoly problem. This approach is good public policy for the following reasons:

- A fair and understandable concept: trackage rights are not new, they are widely used by railroads, are understood and accepted.
- Corrects the root problem of monopolistic management of certain segments of tracks.
- Self-enforcing concept: trackage rights do not require a governmental bureaucracy for implementation. The competitive forces of the marketplace will assure the lowest fair rate be set for use of tracks and provision of service. The most successful governmental regulatory policies are those which are self-enforcing.
- Consumer benefits from allowing competition to set the lowest freight rate rather than incurring the additional expense of an expanded governmental bureaucracy which may or may not accomplish the same outcome.
- Increases the rationale for State Public Utility Regulatory Commissions to accept the costs of delivered fuel in electric rate proceedings.
- Does not amend the Staggers Act and therefore does not involve re-addressing issues inherent in that legislation.

The bill being considered by your committee, S. 2417, would be one way of achieving trackage rights and doing away with the present monopoly structure. Over the coming months, Grace looks forward to working with the Committee to determine how the basic self-enforcing provision of this approach can best be framed in legislation. We urge the committee to consider S. 2417 favorably.

I would be happy to answer any questions you may have.

ATTACHMENTS

A. Details on costs of coal delivery from Colowyo Mine to Utility customers.

B. Table of 1983 Colorado Coal Production, including captive production.
Map of Western Colorado showing rail lines of D&RGW and UP with general location of coal mines.

C. Table of 1983 Utah Coal Production, including captive production.
Map of Utah showing rail line of D&RGW with general location of coal mines

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ATTACHMENT A - PART I

COAL SUPPLY TO CENTRAL POWER & LIGHT

The Colowyo Coal Company long-term contract with Central Power and Light Company of Corpus Christi, Texas, specifies that 1.5 million tons ± 10% be purchased each year. CP&L have been taking the minimum amount due to the excessive rail costs of the coal.

The additional coal required by CP&L is purchased annually. Last spring, CP&L issued a purchase announcement for 220,000 tons of coal. Bids were solicited from a large number of coal producing companies, and responses were received from 36 companies. These included mines in South Africa, Colombia, Poland and British Columbia, as well as eastern and western mines of the United States. Of the producing mines responding to the announcement, Colowyo presented the lowest bid f.o.b. mine. However, Colowyo placed 14th in the cost of coal delivered to the CP&L plant. The contract was awarded to an underground mining operation in southeastern Colorado, to which there is competitive rail shipment. Two railroad carriers submitted competing bids for this traffic and it was the competition between these two carriers that allowed this decision to be made. Although, the length of haul is approximately 300 miles shorter than that from Colowyo, the rail rate was sufficiently low to more than offset the relatively high cost of the underground mined coal involved.

What was disheartening from this bid analysis was the following information revealed to us from CP&L: A surface mine located in the mountainous terrain of British Columbia produces a similar quality of coal as Colowyo. This mine can produce the coal, transport it by truck to a rail loading facility, transfer it to rail and transport it from the mountains to Vancouver, where it is transferred from the railcar to ground storage, or directly into ocean-going vessels. From

Vancouver the coal is transported down the west coast of the North American Continent to the Panama Canal and on up through the Gulf of Mexico to the Port of Corpus Christi, Texas. The coal is transferred from the ship to rail and taken 100 miles to the power plant at Coleto Creek. This coal was quoted at a lower delivered price than our coal which is placed in a unit train to Colorado and never rehandled until it is dumped into the hopper bin feeding the plant at Coleto Creek.

CP&L received bids from coal operations in South Africa, Poland and Columbia. All of these bids, which included shipment to the Port of Corpus Christi, ranked high on a competitive basis.

ATTACHMENT A - PART II

COLOWYO COAL MINE RAILROAD SPUR LINE FOR COAL SHIPMENT

In 1972, with the decision to design a major surface mining operation at the site of the Colowyo mine, it was necessary to include a plan for the long-term shipment of coal.

After assessing the alternatives, truck haulage and overland conveyor systems to existing rail lines, it was decided to build a railroad spur connecting the mine and the D&RGW tracks.

Acquisition of the right-of-way and the design of the 31 mile spur line extended over several additional years. The line was completed in 1979. (See attached map.)

The spur was a joint project of Colowyo, Empire Energy Co., and later on, the Northern Coal Co. These companies, are responsible for the maintenance of the spur line, including roadbed, switches, loading facilities, etc.

In late 1983 the six mile segment of the spur line from the D&RGW tracks to the Empire Mine was sold to a holding company at the same address as the D&RGW. This sale came about since Empire and Northern Coal wanted to recover their remaining investment in their segment of the spur.

The sale to the holding company was for an amount equal to the actual 1977 construction cost.

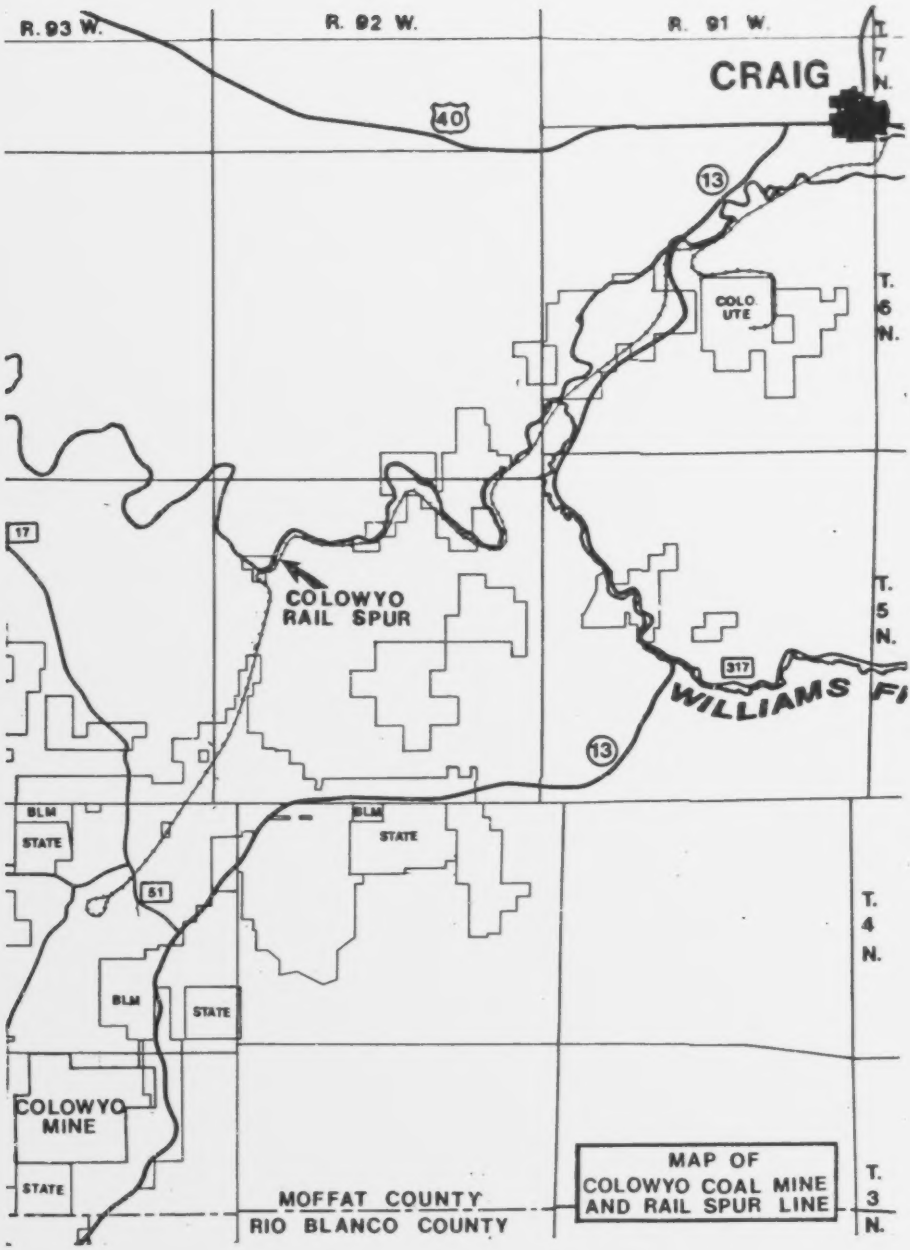
After this sale, the D&RGW determined that a fair rail rate for coal from the Colowyo mine to the Colorado-Ute Power Plant at Craig, which is approximately 23 miles north on the Colowyo spur line (see attached map), was 11 cents/ton mile.

This rate is excessive. The majority of the track used in the haul is still owned and maintained by the coal mine operators. The rail cars and loading and unloading facilities are owned by the mine or the utility. All that D&RGW provides for this rate is: two locomotive engines, a caboose, train crews, switching service, and continued amoritization of the debt for the recently acquired 6 miles of track.

It is estimated that this rate yields revenues to D&RGW at 400% of their costs of providing the service and represents a rate of return on their facilities amounting to 100% annually.

The only other option available for coal deliveries to the Colorado-Ute plant is over-the-road haulage by truck. This option is highly undesirable because of the adverse impacts which would occur on the public uses of State Highway 13, which is the only road connecting the mine to the Town of Craig and the power plant.

If the trackage rights inherent in S.2417 were available at this time, competitive bids would have been received for these coal shipments, and we are convinced they would show a considerable saving when compared to the 11 cents/ton mile rate. Trackage rights are necessary in order to assure access over the D&RGW system to the Colowyo spur and the interconnect between the spur and the railsiding at the utility.


R. 93 W.
R. 92 W.
R. 91 W.
CRAIG
40
13
COLO UTE
T. 6 N.
17
COLOWYO RAIL SPUR
317
WILLIAMS FI
T. 5 N.
BLM
STATE
51
T. 4 N.
COLOWYO MINE
MOFFAT COUNTY
RIO BLANCO COUNTY
MAP OF COLOWYO COAL MINE AND RAIL SPUR LINE
T. 3 N.

ATTACHMENT B

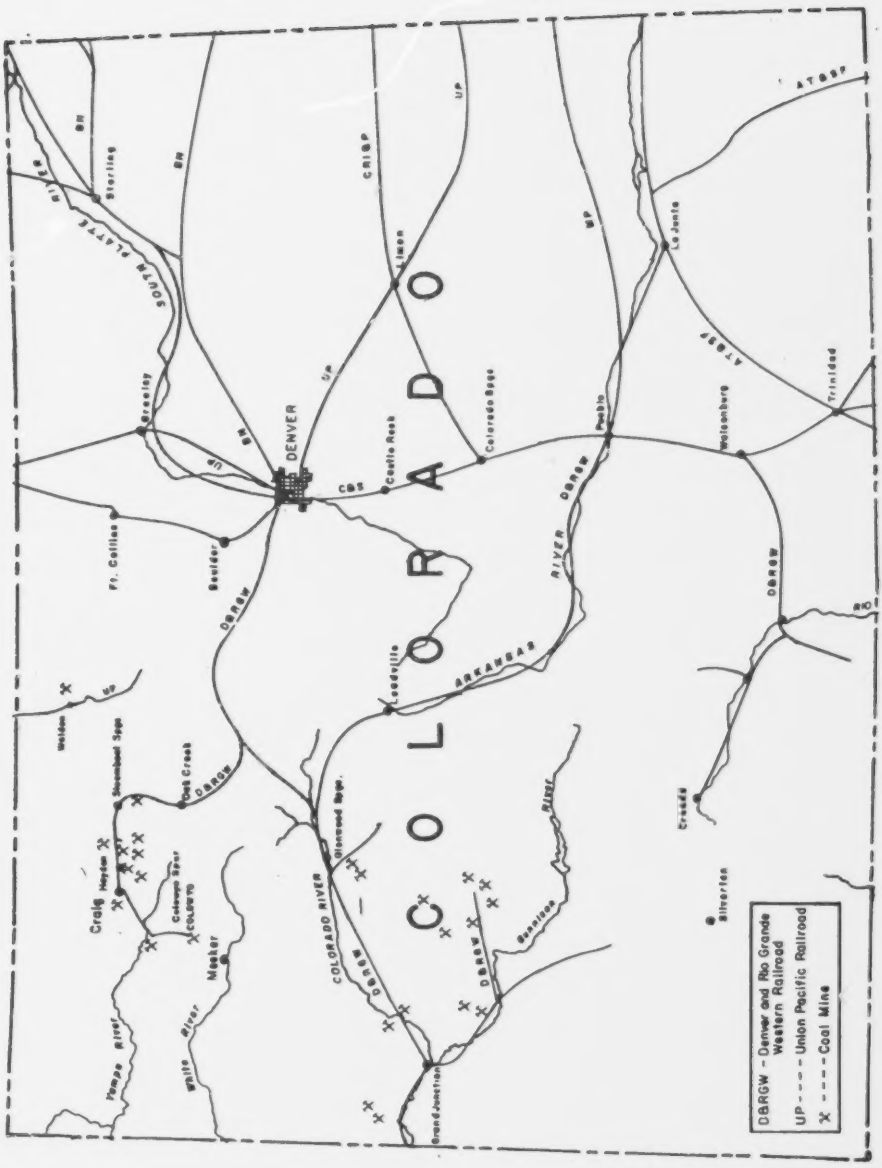
Colorado Coal Production in 1983

And Its Relationship To

Competitive Rail Transportation

	(Million Tons)
State Wide Production	16.741
Production for Mine-Mouth Power Plants *	3.711
Production Dependent Upon Transportation (Common Carrier) For Reaching Markets	13.030
Production Accessible to Competitive Transportation	.381
Production Captive to a Single Railroad (Monopoly Transportation)	12.848
% Of Total Colorado Production That Is Captive To Monopoly Transportation:	78%
% Of Colorado Production Dependent On Common Carrier That Is Captive To Monopoly Transportation:	97%

* This coal production is hauled by either dedicated railroad (single purpose and non-common carrier) or off-road trucks on private haul roads to electric power generation plants.


COLORADO
DENVER
DBRGW - Denver and Rio Grande Western Railroad
UP - - - - Union Pacific Railroad
Coal Mine
Craig
Meeker
Walden
Steamboat Spgs.
Oak Creek
Colorado Spgs.
Florence
Canon City
Pueblo
Walsenburg
Trinidad
La Junta
Colorado Springs
Castle Rock
Limon
Boulder
Ft. Collins
Greeley
Sterling
Grand Junction
Gunnison
Salida
Leadville
Silverton
Crested Butte
Colorado River
Arkansas River
White River
Yampa River
Gunnison River
South Platte River
DBRGW
UP
CRIPP
ATSF
BN
CBQ

ATTACHMENT C

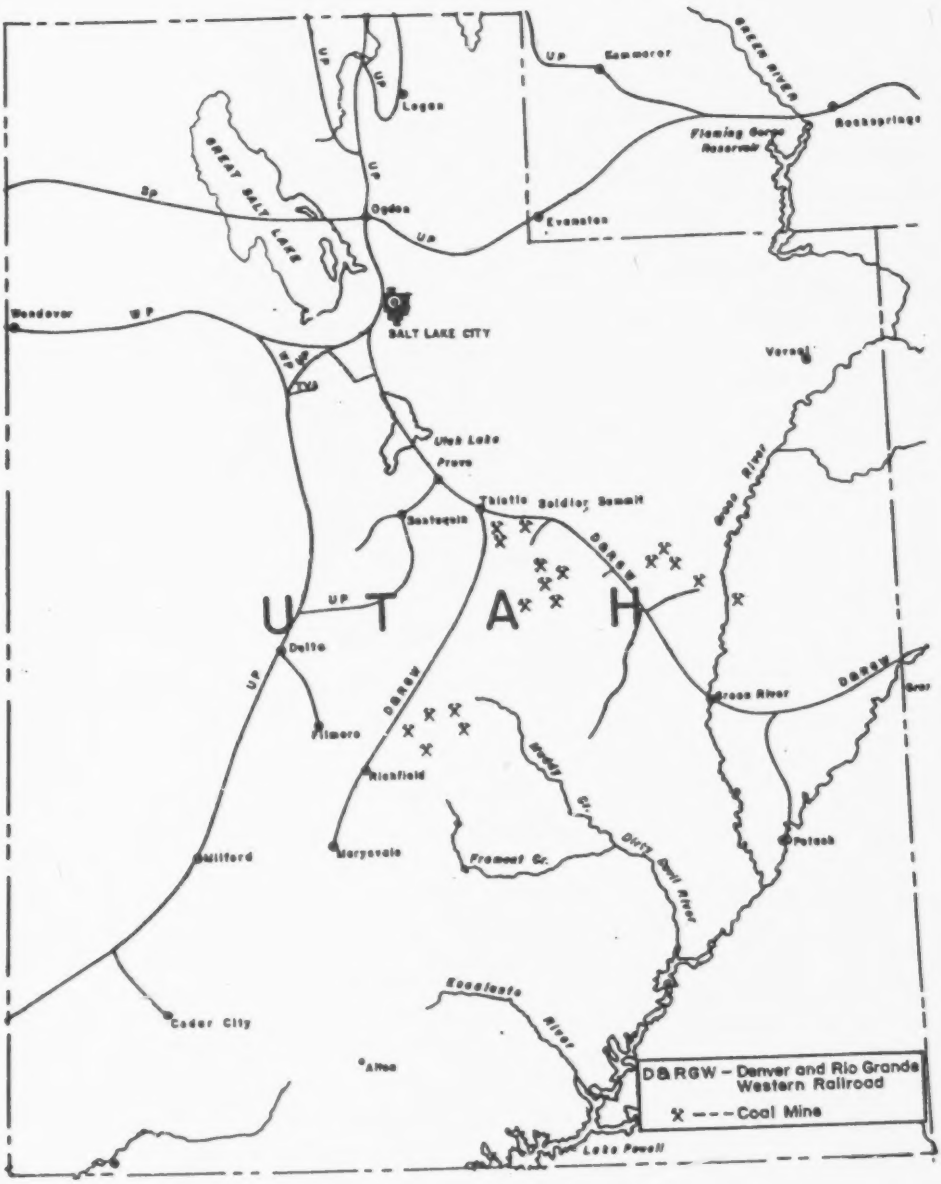
Utah Coal Production in 1983

And Its Relationship To

Competitive Rail Transportation

	(Million Tons)
State Wide Production	11.982
Production for Mine-Mouth Power Plants *	2.176
Production Dependent Upon Transportation (Common Carrier) For Reaching Markets	9.806
Production Accessible to Competitive Transportation	———
Production Captive to a Single Railroad (Monopoly Transportation)	9.806
% Of Total Utah Production That Is Captive To Monopoly Transportation:	82%
% Of Utah Production Dependent On Common Carrier That is Captive To Monopoly Transportation:	100%

* This coal production is hauled by either dedicated railroad (single purpose and non-common carrier) or off-road trucks on private haul roads to electric power generation plants.


UP
Logan
Ogden
Evanston
Kemmerer
Rocksprings
Flaming Gorge Reservoir
GREEN RIVER
GREAT SALT LAKE
SP
Wendover
WP
SALT LAKE CITY
Vernal
Utah Lake
Provo
Thistle
Soldier Summit
Santaquin
DRGW
Grand River
U T A H
Delta
Fillmore
Richfield
Grass River
Price
Milford
Marysvale
Fremont Gr.
Muddy Cr.
Dirty Devil River
Escalante River
Cedar City
Alton
Lake Powell
D&RGW – Denver and Rio Grande Western Railroad
Coal Mine

Senator SIMPSON. Well, thank you so very much. I apologize for being late, but I knew things were in good order with the Senator from Arizona and his presentation of a thoughtful piece of legislation.

I know, also, Senator Baucus, my colleague from the north in Montana, has, I believe, a statement he wishes to make. Max, did you have a comment?

Senator BAUCUS. Mr. Chairman, I have a statement. I ask that it be included in the record. Let me just quickly summarize it.

Senator SIMPSON. Sure.

[The prepared statement follows:]

PREPARED STATEMENT OF SENATOR MAX BAUCUS

Mr. Chairman, I want to thank you for your efforts in making this hearing possible. I also want to commend my colleague from Arizona, Mr. DeConcini, whom I joined in sponsoring S. 2417.

The Consumers' Rail Transportation Antimonopoly Act aims to restore badly-needed competition to the railroad industry—competition in areas of the country where shippers of bulk commodities are "captive shippers."

Montana is a prime example of an area where shippers moving grain, coal, and lumber are captive to one railroad.

Montana's relationship with Burlington Northern has been stormy since the enactment of the Staggers Act. We have worked hard to resolve our differences. Recently, I am pleased to say, the State of Montana and Burlington Northern reached an agreement over the future of the Geraldine branch line—a vital link for grain shippers in Central Montana. This agreement also precludes any further branch line abandonments for the next three years.

This settlement is important for the development of Montana's economy—which is heavily dependent on Burlington Northern to move our goods to market.

We now must turn our attention from branch line abandonments to the rates we pay as captive shippers.

When Congress passed the Staggers Act in 1980, we expected the Interstate Commerce Commission to protect captive shippers from dramatic rate increases where no competition existed to keep rates down. Unfortunately, the ICC is overlooking the plight of captive shippers in ruling after ruling.

There is little doubt why captive shippers of bulk commodities are interested in this legislation.

Coal shippers move 2 out of every 3 tons of coal by rail. And 85% of railroad coal tonnage is captive to a single rail carrier.

With over 50% of the country's electricity produced by burning coal, every energy consumer has a stake in the coal shipping rates.

Captive grain shippers in Montana appealed for help from exorbitant rail rates over three years ago with the ICC. Yet, no action has been taken by the ICC. In April of this year, I asked the ICC how much longer Montana grain shippers would have to wait for action. Their answer was that no action would occur until sometime after a decision on coal rate guidelines—which is not expected until late next year.

Mr. Chairman, I ask unanimous consent that copies of my correspondence with the ICC and their responses be included in the record.

Congress must take action to prevent this type of delay. Captive shippers deserve to have some protection from high freight rates.

There are two ways to protect captive shippers from unfairly high rates. You can regulate rates or you can foster competition.

S. 2417 does not attempt to impose any new regulations over rates. It does attempt to foster competition and, thereby, moderate the exorbitant rates captive shippers now face.

I again want to thank the Chairman of the Committee and Senators Simpson and DeConcini for bringing this important issue to the Judiciary Committee. I also want to thank those testifying today for impressing upon us the need for this legislation. In particular, the National Grain & Feed Association, the National Association of Farmer Coops, the Fertilizer Institute, the National Association of Wheat Growers and the Western Fuels Association.

I look forward to hearing the views of both the proponents and the opponents of the bill.

MAX BAUCUS
MONTANA

WASHINGTON D.C.
(202) 224-2651
MONTANA TOLL FREE NUMBER
1-800-332-6106

United States Senate
WASHINGTON, D.C. 20510

June 6, 1984

The Honorable Reese H. Taylor
Chairman
Interstate Commerce Commission
Washington, D.C. 20423

Dear Mr. Chairman:

I have reviewed with some interest the written response to my question submitted to the ICC at the April 4, 1984, Transportation Appropriation Subcommittee hearing concerning the McCarty Farms Petition (Docket No. 37809). I remain concerned that the long delay in this case will continue to adversely effect the grain shippers in Montana and elsewhere.

In order that I might understand more fully why this delay has occured, I would appreciate receiving your response to the following questions:

1. What is the current schedule for developing the proposed new maximum rate guidelines in Ex Parte 347 (Sub-No. 1)? Please include in your response a calendar for completion of milestones in this matter.

2. How many staff members are currently working on Ex Parte 347 (Sub-No. 1)?

3. What could be done to speed up the action in Ex Parte 347 (Sub-No. 1)?

4. Which staff person will be responsible for making a recommendation to the Commission on whether the coal rate standards will be appropriate for non-coal proceedings? By what date will this recommendation be made? What will be the procedure and schedule if it is determined that the coal rate standards are inappropriate for non-coal proceedings?

Thank you for your attention to this matter. I would appreciate receiving your response by June 22, 1984.

With best personal regards, I am

Sincerely yours,

Max Baucus

BILLINGS (406) 657-6790 | BOZEMAN (406) 586-6104 | BUTTE (406) 782-8700 | GREAT FALLS (406) 761-1574 | HELENA (406) 449-5480 | MISSOULA (406) 329-3123

Interstate Commerce Commission
Washington, D.C. 20423

1984 JUL 13 PM 2 15

JUL 11 1984

OFFICE OF LEGISLATION
AND GOVERNMENTAL AFFAIRS

Honorable Max Baucus
United States Senate
Washington, D.C. 20510

Dear Senator Baucus:

Ex Parte No. 347 (Sub-No. 1), Coal Rate Guidelines, addresses one of the most difficult and complex issues facing the Commission--the establishment of maximum rate guidelines for captive coal. The proceeding was initiated in 1978. Since that time several possible guidelines have been evaluated and rejected. In February of 1983 we proposed a new approach for resolving the maximum rate issue. Comments were received in July 1983. These comments are being carefully evaluated to ensure that the interests of shippers and carriers are fairly balanced.

There are approximately seven staff members involved in Ex Parte No. 347 (Sub-No. 1). Two of these are devoted to the environmental and energy analysis. The remaining two are acting primarily as reviewers and staff resources. These individuals are proceeding as fast as possible in developing policy approaches which meet our regulatory mandates.

The staff completed its review of the comments in February and briefed the Commission in March and April on their content. In addition, the staff has developed various options for resolving some of the problems raised by the parties. They will now develop primarily recommendations and brief the Commission again in July and August. The Chairman plans to call for oral argument in September and a Commission conference in October to discuss the recommendations. After that conference, preparation of a final decision will begin. A draft final decision in this proceeding is expected to be completed by November with a final vote before the end of the year.

In view of the complexity of the case there is really little that can be done to expedite the decisionmaking process. This proceeding is already designated as one of the Commission's highest priorities.

With regard to your question on expanding the guidelines to other commodities, this decision will be made by the Commission. They will, of course, rely on comments by the General Counsel, the Office of Proceedings, the Bureau of Accounts and the Office of Transportation Analysis in making this decision. The Commission has made it clear that in the event a decision is made to apply the maximum rate policy to commodities other than coal, opportunity will be afforded affected parties to address the propriety of such action.

Please let me know if I can be of further assistance in this matter.

Sincerely,

Janice M. Rosenak
Director

Senator BAUCUS. Those of us in the Northwestern part of the country are probably more concerned about the problem of captive shippers than are Senators and Members of the House from other parts of the country, for one simple reason. We do not have as much competition in surface transportation as other parts of the country.

We do not have barge traffic; we do not have many railroads. We do not have seaports. Essentially, we rely very much on a central mode of transportation for bulk commodities, one railroad.

Now, there is another railroad in Montana, the Union Pacific, but it has a very short line in the State. Essentially, there is only one railroad in the State, the BN. I know that is basically the case in other parts of the country as well.

It is our belief that the Staggers Act probably generally went in the right direction insofar as it began to deregulate the railroads. But the problem is it went too far in that direction when it comes to captive shippers.

It is our view that the ICC would pay more attention to the captive shipper problem than it has, and the main point of this hearing, as I see it, is to address that core question. The bill that Senator DeConcini and others have proposed, I think, is a good first step in addressing that question.

How do we either force the ICC to do what it should have done, or how do we address the question some other way? It is our hope to address it not so much by regulation, but rather through the antitrust laws, which is the main thrust of this legislation.

I hope that all witnesses address the question very conscientiously, very directly, very candidly because it is a problem that all of us not only face now, but because it is such a severe problem for us and because it pushes up freight rates so much, we are going to keep addressing it until we solve it.

We are not going to have a hearing today and then forget about it. We are going to keep our eye on the ball. We are going to keep focusing on this question because it is so crucial to our part of the country.

I want to thank you, Mr. Chairman, for holding these hearings because it is a necessary question that has to be addressed. Thank you.

Senator SIMPSON. Thank you, Max, and I certainly concur in what you say.

I have an opening statement. I will present that into the record.

[Prepared statement follows:]

OPENING STATEMENT OF SENATOR ALAN K. SIMPSON

This hearing will come to order.

Good afternoon to you all. Thank you for coming here today. This hearing is on S. 2417, the Consumers Rail Transportation Antimonopoly Act, introduced by my colleague, Senator DeConcini.

This legislation would provide a remedy under the antitrust laws for the situation where a rail carrier would take unfair advantage of a "captive shipper." A "captive shipper" is one who has no alternative means to get his goods to market. Certainly that can very well be the case with many of our coal producers, with agricultural products, with chemical products—with virtually every product that is shipped in bulk, the "captive shipper" problem can exist.

This legislation is restricted to railroads—and railroads are unique in the existence of "captive shippers." For waterborne commerce, any vessel is free to ply the

various waterways of this country. Similarly, the highways and roads of this country are open to all—and with trucking deregulation in place, there is a growing and rather healthy competition. Once a railroad is built, however, and shipment by truck is not feasible and there is no convenient waterway—the only alternative may be to build another railroad—an expensive alternative.

Oddly enough, that is almost the assumption made under the limited regulation of railroad rates that is left in the aftermath of the 1980 railroad deregulation legislation, commonly called "Staggers Act." That legislation left the great bulk of railroad rates subject to the demands of the marketplace—relying on competition to restrain the rates rather than the intervention of a Government agency. Special provisions were contained in the Staggers Act to deal with "captive shippers." The continued attention of the Interstate Commerce Commission was to be focussed on "captive shipper" situations because there would not be the vigorous competition necessary to act as a restraint on rates.

Unfortunately, the ICC regulations applying the "captive shipper" provisions of the Staggers Act have proven inadequate to protect the shippers from unreasonably escalating rate charges. The ICC regulations are based upon the costs of providing the transportation—yet the ICC formulation results in no effective control on rates. One study of railroad rate regulation after 1980—"Railroad Revenue Adequacy: A Critical Analysis," by E.S. Robson and Anne Evan Foudray—concludes in part that the ICC "has allowed accounting conventions which vastly understate income and overstate investment base. . . ." While the report goes on to acknowledge that the ICC has proposed modifications to these accounting conventions, at the same time they have proposed to value the investment base at replacement cost. In effect, rates are evalued against the cost to build a competing road alongside the railroad whose rates are being examined!

The inadequacy of the ICC regulation has been acknowledged by others. Legislation to revise the ICC formulation—S. 1082, introduced by Senators Huddleson and Ford—is now pending in the Commerce Committee. That legislation is viewed by some as a dangerous reopening of the question of railroad rate deregulation. They fear that revisiting the Staggers Act could lead to attempts at "re-regulation" rather than continued regulation.

One of the virtues of the present legislation, S. 2417, is that it does not require a new round of deregulation debate. By creating an antitrust violation for the abuse of the "captive shipper" situation, we have created a mechanism that does not require the intervention of a Federal agency. An aggrieved party can simply "take his case to court" and, if wronged, receive relief in the form of damages or injunction or whatever the court deems appropriate. The threat of litigation and the threat of being found liable for damages acts as a very strong deterrent against abusing "captive shippers."

Our purpose here today is to begin the process of evaluating this approach as embodied in S. 2417. We want to begin the debate on the "pros and cons" of such an effort. So without further elaboration on my part—let us proceed to the first panel of witnesses.

I would remind each of you that the "five minute rule" is in effect for this hearing. Each of your submitted statements will be placed in the record in full—please make every good effort to limit your remarks to five minute and summarize your prepared testimony. That will allow us to proceed expeditiously and allow more time for questioning.

The first panel is Ira McKeever of W.R. Grace & Co.; Professor Scott Atkinson of the University of Wyoming; and Dr. Stephen Anderson of the Consumer Energy Council of America.

Welcome, gentlemen.

Senator SIMPSON. I would just briefly comment that indeed, it is not just a provincial thought because this is going to affect others, but the principal effect of it is in the West, especially in a State that I represent where we now are the second largest coal producing State in the United States, which shocks people, especially my good colleague from West Virginia, Jennings Randolph.

It is a startling fact, but it is the truth, and yet we have this situation with the captive shipper. And then when people try to nail us in the West on the issue that our severance tax is high, and therefore people are getting a bum rap in Detroit, that is not why the utility rate is high in Detroit.

The reason the utility rate is high in Detroit is because of transportation costs. It is about two bits a month as to what the severance tax for Wyoming does in a utility bill in Detroit. So that is a bum rap and that will not work.

I do not think any of us has an intent to reregulate, but certainly we are going to do something with the ICC. The ICC formulation results in no effective controls on rates.

We have studies, and I know you are going to share with us some of that, but what an absurd situation we have. The ICC has proposed modifications to their accounting conventions at the same time they propose to value the investment base at replacement cost, which means that rates are evaluated against the cost to build a competing road along the railroad whose rates are being examined.

No wonder they are confused about that. We want to lead them out of that confusion. I think we do, anyway. So, with regard to the virtues of this legislation, I think it is a thoughtful piece. It does not require a new round of deregulation debate.

By creating an antitrust violation for the abuse of the captive shipper situation, we have created a mechanism that does not require the intervention of a Federal agency. The aggrieved party can simply take his case to court and, if wronged, he can receive relief in the form of damages or injunction or whatever the court deems appropriate.

The threat of litigation and the threat of being found liable for damages acts, I think, as a very strong deterrent against abusing captive shippers.

So those are my own feelings about this issue, and I believe our next witness—I think you have been advised that we do have the 5-minute rule in effect at the hearing, but it is a pleasure and an honor to recognize and greet our professor from the University of Wyoming, Prof. Scott Atkinson.

I have read some of your previous remarks and thoughtful treatises. It is nice to have you here.

STATEMENT OF PROF. SCOTT ATKINSON

Professor ATKINSON. Thank you very much, Senator Simpson. I am an associate professor of economics, and I am also director of the institute for policy research at the University of Wyoming.

I would like to preface my remarks with the statement that my views do not necessarily—although hopefully they would—represent those of the University of Wyoming or any agency of the State. However, I would like to speak on this issue as a professional economist and academician and one who has studied the area of transportation and resource economics.

S. 2417 addresses important shortcomings in the Staggers Act regarding captive shippers, as Senator Simpson has just indicated, and if enacted into law, I estimate that S. 2417 would significantly increase competition and lower transportation charges, particularly out of the Powder River basin of Wyoming.

The captive shipper provision of the Staggers Act has failed to increase competition and reduce rail transportation prices in monopolized markets. In fact, I would argue—and I would like, if pos-

sible, to expand on this a little bit later—that this provision has gone the other way. It has encouraged monopolization and encouraged higher prices, the way it has been interpreted by the ICC.

If we examine coal sales from Wyoming's Powder River basin—and this is an area that I have studied for the last 3 years quite intensively—until July of this year, the sole rail access to that basin was provided by one railroad; namely, Burlington Northern.

This was exactly, then, the monopoly market situation that you have hoped to address with S. 2417. Using data on sales from the Powder River basin to the shippers of this coal, and 97 percent of these are utilities—basically, we are talking about a market comprised of electric utilities—I have estimated that over that 1980–81 period, Burlington Northern exercised substantial monopoly power by charging higher than competitive rail rates. Further, rail rates would fall significantly, up to around 16 percent and that coal sales would rise significantly—and this is quite an astounding figure to me—up to around 30 percent in the more distant markets if competition in coal shipping prevailed.

By the way, for these distant markets, you are exactly right—our final delivered prices of coal are comprised up to 75 percent by rail rates. So, for example, people in Chicago are paying for rail rates to quite a great extent.

So, if vigorous competition were introduced, we would find these kinds of increases in coal sales and reductions in prices. However, under the market dominance provision of the Staggers Act, there is not one shipper—not one utility—which buys Wyoming coal which could qualify as a "captive shipper," as now interpreted by the ICC. Even though they were served by a single rail line until July 1984, none of them could qualify as captive shippers. Therefore, they could not appeal to the ICC for rate relief.

Recently we saw the Chicago Northwestern come into the Powder River basin—and this was an entry that was postponed for a great deal of time through litigation and repeated appeals by Burlington Northern. The Chicago Northwestern entered through the mandate of the ICC, and they purchased one-half of Burlington Northern rail lines through the Powder River basin for $76 million rather than the about $96 million which Burlington Northern demanded.

But when they entered, we saw significant reductions in rail rates to many, or at least to a number of utilities which were buying coal out of the Powder River basin. S. 2417 would have automatically required these parties to get together, under threat of litigation.

Under S. 2417, the parties would get together and reach a reasonable agreement as to reasonable terms and avoid the costly, time-consuming delays which they have faced. The entry of Chicago Northwestern has caused substantial reduction in rail rates, up to $5 to $6 per ton, it has been estimated, for Arkansas Power & Light which recently negotiated with them. And this agreement is estimated to save $211 million through 1986, just a few years away.

Wisconsin Public Service has also reached an agreement with Chicago Northwestern. This is estimated to save them $100 million at their Weston plant over the next 15 years, once this plant actually comes on line.

Significant reductions can be expected for other utilities, particularly the Texas utilities which have been hit with very heavy rate increases in the last few years.

So, basically, the experience with the Burlington Northern and Chicago Northwestern in the Powder River basin, I think, can be generalized to talk about other commodities where a single rail line provides sole access to a shipper's customers.

Senator SIMPSON. Thank you very much. I do appreciate your observing the time, and thank you for your thoughtful review, very capably done.

The next member of the panel is Dr. Stephen Andersen, director of research, Consumer Energy Council of America, in Washington. Please begin.

STATEMENT OF DR. STEPHEN O. ANDERSEN

Dr. ANDERSEN. Thank you, Mr. Chairman and members of the committee. My name is Dr. Stephen Andersen and I am director of research of the Consumer Energy Council of America. I appreciate the opportunity to appear here today.

CECA is a broad-based coalition of major national consumer, labor, farm, public power, rural electric cooperative, senior citizen, urban, and low-income organizations. It was established over a decade ago to bring the consumer view to national energy policy.

The Consumer Energy Council is convinced that legislative action is necessary to restore the proper balance between railroads and consumers. My testimony reviews the consumer interest and comments specifically on S. 2417.

The provisions of the Staggers Rail Act of 1980 which protected shippers were weak to begin with, and the Interstate Commerce Commission has limited them even further. Shippers of bulk commodities like coal and agricultural commodities are frequently captives of the railroads because they often have no alternative means to transport their goods.

With fuel adjustment clauses translating coal transportation price increases directly into electricity price increases, and with electric utility bills constituting over half of the Nation's expenditures for energy used in the home, railroad deregulation has created the potential for drastic overcharging.

I am sure other witnesses today will mention that. I would like to concentrate my time on the impact on farmers. The farm sector will experience drastic consequences of railroad deregulation. Unlike electric utilities, however, farmers are unable to pass rail rate increases along to the customers. This is because farmers are caught in a price squeeze.

If a single railroad controls the route to market, that railroad can increase prices to take away profits that rightfully belong to the farmer. The railroad can also increase the cost of shipping farm inputs like fertilizer and feed grain to farmers. Thus, a farmer is forced to pay more to produce and is paid less for products. My written testimony discusses this in greater detail.

I will use the rest of my time to comment on S. 2417. S. 2417 is intended to prevent monopoly price exploitation of captive shippers

by allowing those shippers to provide their own rail stock and use the rail bed at a fair price.

In many cases, we believe that this legislative solution could be effective as a countervailing force to the monopoly power of the railroad. Large companies with predictable and secure shipping needs, like coal companies and electric utilities, can take advantage of the act's provisions.

They could make the administrative investment before the ICC to qualify to use the rails, and they could afford to buy the rail stock. For these shippers, rolling stock ownership could be affordable because they need to supply coal on a regular basis year around.

However, additional legislation is necessary beyond S. 2417 to restore economic balance. Many shippers do not make periodic fixed-point shipments. Farmers and manufacturers, for example, could not afford either the administrative expense or the cost of the railroad equipment. These shippers would find no relief from this legislation.

We would also add that there remains a strong argument that railroads be operated as a single corporation, owning enough capital to serve their customers efficiently and economically. Under this historic monopoly ownership, of course, they must be regulated.

The access to the rails proposed in S. 2417 also must be complemented with changes to the 1980 Staggers Rail Act to protect captive shippers against rapid rate increases because they cannot quickly acquire the railroad rolling stock even if they had the financial means.

For example, if there were a world economic recovery that increased the currently depressed agricultural prices, it would be necessary for farmers to move their goods to markets, particularly ports, very quickly. In these circumstances, farmers would find that the railroads could raise the rates and capture the profits that rightly belong to them. They would have no alternative, especially in the short run, but to pay. They are in no position, because of their already exorbitant debt, to make this kind of investment.

Other amendments should be considered to S. 2417 to provide flexibility for the use of locomotives and cars that are owned by shippers. For example, if an electric utility owned an excess capacity of boxcars or hoppercars, they might not be able to haul bulk commodities for other companies without securing special designation as a railroad. This could prevent even back haul of bulk commodities from powerplants towards the coal mine.

Alternatively, if this legislation allowed rolling stock owners to haul freight without regulation, this might become a loophole for railroads to evade even the inadequate regulation that they now have.

In summary, S. 2417 provides part, but not all, of the desperately needed reform. It could prove valuable as part of a bigger legislative package that would restore protection to captive shippers, encourage increased railroad efficiency, and provide flexibility for shippers.

43-746 O - 85 - 2

CECA thanks you for taking the initiative in trying to get the railroads back under control and for inviting me to testify.

[The prepared statement follows.]

CONSUMER ENERGY COUNCIL of AMERICA
2000 L Street NW Suite 320 Washington DC 20036-202-659-0404

Testimony of

Dr. Stephen O. Andersen

Director of Research

of the

Consumer Energy Council of America

Mr. Chairman and Members of the Committee:

My name is Dr. Stephen O. Andersen and I am the Director of Research of the Consumer Energy Council of America (CECA). I appreciate the opportunity to appear before you today on behalf of CECA, the nation's leading public interest energy policy organization. CECA is a broad-based coalition of major national consumer, labor, farm, public power, rural electric cooperative, senior citizen, urban and low income organizations established over a decade ago to represent the consumer point of view in national energy policy issues.

The Consumer Energy Council of America is convinced that legislative action is necessary to restore proper management of the railroads and to end price abuse by railroads.

My testimony reviews the consumer interest in railroad ratemaking and comments specifically on S.2417.

Introduction

The provisions of the Staggers Rail Act of 1980 which protected shippers were weak to begin with and the Interstate Commerce Commission (ICC) has eviscerated them even further. Legislative action and a strong message to the ICC are necessary if balance is to be restored between meeting the needs of the railroads for adequate revenues and meeting the needs of the nation's consumers for affordable electricity. At the time of the passage of the Staggers Act, the Consumer Energy Council of America called for stronger provisions to the Staggers Act and closer regulation of railroad coal rates to protect the nation's residential energy consumers. The need for these stronger protections is even greater today than it was in 1980. Consumers of electricity are captives of the railroads because coal, which is the single largest source of electric power generation, is almost invariably delivered to local utilities under noncompetitive circumstances.

Shippers of bulk commodities like coal and agricultural commodities are frequently captives of the railroads because they have often no alternative means of transport that is affordable. Over half of all electricity is generated from coal and the vast majority (85 percent) of all coal utilized by utilities is delivered under noncompetitive transportation conditions. With fuel adjustment clauses translating coal transportation price increases directly into electricity price increases, and with electric utility bills constituting over half of the nation's

expenditures for energy used in the home, railroad deregulation created the potential for extremely burdensome increases in residential energy costs. Even worse, these rail rate increases are concealed from consumers as part of their electricity bills. According to CECA's research, failure to act could cost electric consumers even more than the impact of decontrol of natural gas!

In addition to the direct impact of coal rate increases on electric utilities, the farm sector will also experience drastic consequences of railroad deregulation. Unlike electric utilities, however, farmers cannot pass rail rate increases along to customers. The farmer is caught in a price squeeze. Food and fiber prices are established in a world market and these prices are offered for commodities delivered to trade centers. For example, wheat produced in Wyoming might be sold to the Chicago wheat market. Chicago would post prices for wheat delivered to their elevators. Elevators in Wyoming would offer farmers the Chicago price, minus the cost of shipping. The higher the shipping cost, the less the farmer gets. If a single railroad controls the route to Chicago, that railroad can increase prices to take away profits that rightfully belong to the farmer. The railroad can also increase the cost of shipping farm inputs like fertilizer and feedgrain to farmers. Thus, a farmer is forced to pay more to produce and is paid less for the products.

Farmers and other rural businesses are being hurt by deregulation in other ways too. Deregulation has allowed railroads to abandon branchlines quickly, cancel joint rates and reciprocal switching agreements, and refuse to provide shippers and receivers with liability protection. It has encouraged secret contracts that favor one business over another and that make remedial action virtually impossible because rate abuses cannot be documented. Figure 1 outlines these effects to farmers and rural communities.

Figure 1

The Effect of Railroad Rates on Farmers and Rural Communities

The Electric Connection

- Electric rate increases resulting from increased rail rates for coal are passed on by electric utilities to farmers and other customers.
- Farmers use substantial amounts of electricity for irrigation, crop drying, greenhouses, automated feeding, dairy equipment and refrigeration.
- Higher electric rates increase production costs but farm product prices do not increase enough to maintain parity.
- Reduced farm profits and higher electric bills for everyone result in less spending in the local economy. A weak local economy hurts all local residents.

The Freight Connection

- Increased shipping costs lower farm product prices because distant markets set the delivered price and farmers absorb the cost of delivery.
- Increases shipping also increases bulk farm input prices like fertilizers and feedgrains. Farmers are caught between increased costs and lower freight-on-board FOB prices.

- Changes in production costs and farm prices may make existing farm operations uneconoomical. This requires farmers to scrap specialized capital and invest in new equipment at high interest rates that compound the problem.

In addition to these serious consequences to electric consumers and farmers, consider the overall effects to the national economy. Careless decontrol of monopolies is already having serious consequences in the telephone, airline and energy businesses. Exploitative rail rates slow economic recovery by reducing profits of shippers, increasing the costs of businesses and by reducing the purchasing power of consumers. Because many American products are barely competitive with imports, these price increases will increase imports and decrease exports, worsening our balance of trade and our national deficit.

Legislative Intent and Administrative Betrayal

The Staggers Rail Act of 1980 is widely recognized as a radical break with past regulatory practices. The new approach in Staggers gave the ICC and the railroads a great deal of freedom to allow railroads to raise rates, rationalize service and generally improve the efficiency of their operations. However, one of the central concerns at the time of the passage of the Act was the extent of regulatory protection to be provided to shippers of bulk commodities, such as coal, farm commodities and other bulk commodities. Because these commodities are frequently shipped under monopoly conditions, it was believed that preservation of considerable regulatory control over the market was necessary in order to provide consumers with adequate protection.

Little did anyone realize that the ICC would disregard the minimal protections of the rate provisions of the Staggers Act. In an ongoing round of rulemakings, the ICC is allowing the railroads to increase coal rates up to 15 percent above the rate of inflation every year until they meet a test of revenue adequacy -- a test which will ensure not that the railroads are healthy, but that they are wealthy. If the ICC's generous 15% above inflation solution is extended to other bulk commodities, the railroads will have restored their historic monopoly power to do as they please -- the public be damned.

The ICC has adopted a test of revenue adequacy which every Class I railroad in the nation has failed, even though more than half of the nation's major railroads have been quite healthy for a decade and the industry is generally going through an extremely robust economic period. This declared fictional revenue inadequacy despite actual profitability has been accomplished by a series of rulemakings that choose standards for accounting, cost estimation and revenue needs that inflate the railroads' needs while understating the economic health of the industry. These distortions include the overestimation of the basic capital needs of the industry (replacement cost, inclusion of deferred taxes, use of current capital costs instead of imbedded debt, etc.), the overestimation of costs (use of average industry-wide costs, exclusion of productivity increases from the estimation of costs, etc.), and the choice of the highest possible measure of revenue adequacy (current cost of capital with no consideration of the financial status of the railroads). These regulatory concepts are difficult and mind numbing. The bottom line, however, is simple: these concepts allow the railroads to charge their monopolized customers whatever they want.

The ICC has robbed captive consumers of protection from exploitation by abandoning all effective tests of market dominance and by refusing to establish incentives for railroads to improve their operations in competitive markets. While the

ICC is willing to allow staggering increases in coal rates, it refuses to insure the maximum possible contribution to overall system costs from traffic carried under competitive conditions. Moreover, the rapid concentration of the transportation industry through potential mergers makes the need for effective protection of captive shippers and consumers even more critical.

The Impact on the Consumer

Without quick action there will be an unjustified transfer of wealth from electricity consumers and purchasers of agricultural and manufactured goods to the railroads. Electric rates subject to the fuel adjustment clause are particularly vulnerable because increases for coal haulage can be passed through to consumers dollar for dollar.

Given the rapidly escalating prices for energy and the central role that energy plays in overall price inflation, the deregulation of coal freight rates is particlularly insidious to consumers. The impact on the consumer of an unregulated railroad industry trying to solve all of its financial problems by extracting maximum advantage from its monopoly control over coal hauling and other bulk commodities will be staggering.

Other actions of Congress have unintentionally created a climate favorable to price gouging by railroads. Legislation forcing utilities off other fuels and on to coal permits exorbitant prices in the shipment of coal. So much money has been invested in the relatively new coal-fired power plants that the utilities must stay with coal. In addition, utilities are often unable to borrow money to switch fuels again. This presents an impossible situation for consumers. Absent any competition working to restrain prices and absent any government mechanism to prevent these price hikes, the Congress must take action now to protect American consumers.

The economic harm from excessive rail rates is not linked to a few products or a few locales because these price increases will be passed on to all consumers or will reduce business profit. Consider the case of coal shipments.

Coal, like other bulk commodities, can be shipped at lowest cost by water or rail. Where waterways are not available, a single railroad is often the only option. If the railroad can charge any price it chooses, the railroad can hold coal companies and coal customers hostage. Increases in rail rates are made at the expense of shippers and consumers. Shippers absorb part of the price increase by earning less profit and pass part of the price increase on to consumers.

Electric utilities often purchase coal that can only be shipped by railroad. When the railroad increases its rates, the utility has no transportation alternative and the full price increase is immediately passed on to consumers through fuel adjustment clauses and in periodic rate increases. Because electric utilities are regulated monopolies that are normally charging less than the market will bear, the railraod can actually raise rates so much that they capture not only railroad monopoly profits, but also utility monopoly profits! The ultimate effect is to make utility management and public utility commissions powerless.

Any advantage of capital investment or good management in coal mining or coal using businesses can be captured by the railroads. Railroads can literally drain the profits from businesses at both ends of their rails. When profits are reduced at coal mines, the stockholders, employees and local communities lose. When electric rates increase, businesses lay off workers and consumers have less to spend on other purchases.

The Impact on the Economy

If the railroads continue to be even modestly successful in extracting monopoly profits, the negative consequences will include inflation, unemployment and economic dislocation. Additionally, deregulation would contradict the national energy policy objective of encouraging the use of coal by utilities and industry. Control of acid rain will be made far more costly because coal cannot be economically shipped to the plants best suited to its particular characteristics. This in turn will worsen the lives of miners who are unemployed because high rail rates make their mines inoperable. Finally, it will increase our nation's dependence on foreign energy by dampening the incentive to convert from oil to coal, thereby maintaining our reliance on oil imports.

The Inappropriateness of Railroad Rate Increases

It is ironic that the railroad industry is preparing to exploit energy consumers. The railroads' financial prospects have brightened considerably as a result of energy price increases and recent energy policy decisions. The railroad industry is the beneficiary of energy price increases, which make it more competitive with other transportation modes, and by coal conversion, which has increased its business.

Looking to the future, the volume of business the railroads are likely to do in at least one commodity they monopolize -- coal -- is likely to increase rapidly. The National Academy of Sciences recently predicted a doubling of coal production over the next decade and as much as a five-fold increase by the year 2000. If this improved situation is not adequate for the railroad industry's healthy survival, then another solution needs to be found which does not result in incredible and inequitable burdens for the nation's utility consumers.

Specific Comments on S.2417

The Consumers' Railroad Transportation Antimonopoly Act is intended to prevent monopoly price exploitation of captive shippers by allowing those shippers to provide their own rolling stock and to use the railroad bed at a fair price. In many cases, this legislative solution could be an effective countervailing force to monopoly railroad power. Large companies with predictable and secure shipping needs -- like coal companies and electric utlities -- can take advantage of the Acts' provisions. They could make the administrative investment before the ICC to qualify to use the rails and they could afford to buy the rolling stock. For these shippers, rolling stock ownership could be affordable because they need to supply coal on a regular basis year round.

However, additional legislation is necessary beyond S.2417 to restore the overall economic balance between railroads and shippers. Many shippers who do not make periodic shipments between fixed locations -- like farmers and manufacturers -- could not afford either the administrative expense or the cost of railroad equipment. These shippers would find no relief from this legislation.

There remains a strong argument that railroads be operated as a single corporation owning enough capital to serve their customers efficiently and economically. Under this historic monopoly ownership, the railroads are regulated to prevent price abuse.

The access to rails proposed by S.2417 must be complemented by amendments to the 1980 Staggers Rail Act to protect shippers against rapid rate increases because shippers cannot quickly acquire rolling stock even if they have the

financial means to make these expensive purchases. For example, world economic recovery might increase depressed agricultural prices to reasonable levels. In these circumstances, farmers might quickly need to move commodities to ocean ports. Railroads holding these farmers captive could increase rates and capture profit that rightly belongs to farmers. Farmers would have no alternative but to pay and certainly are not in a position to invest in railroads -- most farmers are debt ridden as it is.

Other amendments should be considered to S.2417 to provide desirable flexibility for the use of locomotives and cars that are owned by shippers. For example, if an electric utility owned an excess capacity of boxcars, they may not be able to haul bulk commodities for other companies without securing special designation as a railroad. This could prevent even the back-haul of freight from the powerplant toward the coal mine.

Alternately, if this legislation allows rolling stock owners to haul freight without regulation (section 9 c), this might become a loophole for railroads to evade even the inadequate regulation they now have.

Proposed Legislative Reform

The Consumer Energy Council of America supports regulatory reform -- legislative and administrative -- that would:

1. ensure that no railroad be allowed to extract monopoly profits;

2. provide a reasonable criteria for the financial health of the railroads;

3. establish a realistic cost accounting methodology to ascertain the financial status of the railroads;

4. ensure that efficiency improvements, not rate increases, form the core of the effort to ensure a viable rail system;

5. provide captive shippers a fair test for determining that they have no reasonable transportation alternatives (market dominance);

6. require that maximum rates for captive commodities take into account the impact on the ultimate consumers;

7. require that the rate increase inflation index be based on actual rail cost increases, adjusted for productivity gains; and stipulate that rates automatically decrease when the inflation index declines; and

8. require that other railroads be granted access and usage of rail facilities, with reasonable compensation, to assume greater competition in cases of captive shippers.

S.2417 provides part, but not all, of this desperately needed reform. It could prove valuable as part of a bigger legislative package that would restore protection of captive shippers, encourage increased railroad efficiency and provide flexibility for shippers. CECA thanks you for taking the initiative in trying to get the railroads back under control and for inviting me to testify today.

Senator SIMPSON. Thank you very much for your thoughtful testimony.

I have just a couple of questions and then Senator DeConcini will have a series of questions. I might ask Professor Atkinson what other factors, in your mind, besides the increased competition for Chicago Northwestern, might account for the dramatic drop in rates from the Powder River basin? I would be interested in your views.

Professor ATKINSON. Well, first of all, if I could get into an answer to that by first maybe just summarizing the evidence of actual drops in rates just a little bit more carefully, then that might lead into an answer to that.

Senator SIMPSON. Do not go too far back, though.

Professor ATKINSON. First of all, there is the Arkansas Power & Light contract, and as I go through this, I think I will answer the question at the same time. There was competitive underbidding by Chicago Northwestern, underbidding of both the Burlington Northern and the ETSI coal slurry pipeline, which has since gone defunct.

Anyway, this was a competitive process where Chicago Northwestern won the contract to deliver 10 million tons of coal per year over the next 20 years. It has been estimated, although the terms of this contract have not been divulged, that there was a $5- to $6-per-ton savings under the Burlington Northern previous rate, and that the total savings is about $211 million, again, through 1986.

So, in addition to Chicago Northwestern, we could say that one of the competitive pressures was the coal slurry pipeline. This is now gone, so this is one avenue which is not there anymore. Of course, barges and other forms of seagoing transportation could not really come into play for the vast amount of Wyoming coal. Some is transported by barge, but there is not a great deal of that.

The second bit of evidence where there has been competition with Burlington Northern is a contract which was recently signed by Chicago Northwestern to deliver 800,000 tons per year to the Wisconsin Public Service Weston plant. It was estimated that $100 million will be saved over the next 15 years.

In addition, there are numerous attempts to negotiate contracts right now between Chicago Northwestern and numerous Texas utilities. Again, they are basically under the stranglehold of Burlington Northern. They are, in fact, under the category of what I would call captive shippers, and yet under the way it is interpreted by ICC, they could never qualify as such.

So I would say the main competitive impetus here is, in fact, from the entry of Chicago Northwestern, the exception being the ETSI pipeline.

Senator SIMPSON. Just one final question addressed to any member of the panel: What other benefits besides lower rates, which I think is alleged perhaps to be the sole reason for this measure—and I do not believe it is, but it is certainly a key one—what other benefits besides lower rates might we see from this increased competition for captive shippers?

Mr. MCKEEVER. I would like to take one shot at that. I think where the shipper now, like a utility, owns its own cars, you would see shorter turnaround time and use of that capital, and therefore

lowering the amount of capital necessary to move the same amount of tonnage in 1 year. I could see better operating conditions from that standpoint.

Senator SIMPSON. Anyone else on the panel care to address that? Yes, sir, Dr. Andersen?

Dr. ANDERSEN. Your legislation would offer a deterrent to price increases, and would also provide competition in services. That might be very useful.

Also, in those cases where a shipper chose to buy the rolling stock and operate that rolling stock, the example would be a useful yardstick of what costs we could expect from the efficient operation of railroads and we could compare that to the railroad rates that were charged elsewhere.

Senator SIMPSON. Do you have any comment, Professor Atkinson?

Professor ATKINSON. In addition to reduced rail rates, we would expect to find an increase in coal sales, and this has a number of very beneficial repercussions. We would increase coal sales; we would increase employment, obviously, of Western coal miners.

We would also increase the employment of railroad people as well because we would have more demand and usage of the railroads; hence, more personnel employed. In addition, and I think this is very important, we would find reduced prices for electric utilities, and hence reduced electricity bills for those consumers throughout the Midwest and Texas.

We would also expect to find lower prices on industrial products which use substantial amounts of electricity. So I think there are numerous extremely important, far-reaching effects, positive increases in economic efficiency, moving prices closer to their bare minimums, which will be experienced by a vast number of people throughout the country and not just simply in Wyoming.

Senator SIMPSON. I thank you very much. I think that is a very important point that we do not become enmeshed in the provincialness of the issue; that it is for the benefit of many other States.

I have a conflict which I related to the chairman of the committee, and therefore the Chair will now be handled by Senator DeConcini and he has further questions.

Thanks, Dennis.

[Senator DeConcini assumed the Chair.]

Senator DECONCINI. Mr. Chairman, thank you, and thank you for your support of this legislation and your interest in it and taking the time from your schedule and your conference to be here with us.

Senator SIMPSON. Do you want to go back to the conference for me?

Senator DECONCINI. No. I would much rather stay here.

Mr. McKeever, currently the ICC has jurisdiction over rail rate-setting. Have you made attempts to have your case addressed by the ICC?

Mr. MCKEEVER. Well, we are a coal mine and the handling of the rail freight has been by the customer or the shipper in this case.

Senator DECONCINI. You do not get involved in that?

Mr. MCKEEVER. That is right.

Senator DECONCINI. Do you know if they have attempted to?

Mr. McKeever. Yes, in the case of Colorado Ute, where the Colorado State PUC jurisdiction is intrastate, the PUC, as I understand it, acted under the ICC guidelines. Otherwise, it is automatically remanded to ICC anyway. So the PUC study and case will be handled under ICC guidelines.

Senator DeConcini. Professor Atkinson, under the Staggers Act, a captive shipper must first qualify as such before being able to receive special relief from the ICC. Is this captive shipper provision of this act reasonable, in your opinion, and does it go far enough?

Professor Atkinson. As I stated earlier, my opinion is that this captive shipper provision is really such a provision that it serves to, in effect, produce the opposite result from which was intended; that is, I would argue that it serves to decrease competition, increase the monopoly advantage of the railroad and, in fact, raise rail rates rather than decrease them.

Senator DeConcini. So from your study that I understand you have there, you do not foresee any shippers qualifying as captive and receiving any special aid from the ICC?

Professor Atkinson. Yes. If I look at all the shippers, and we are talking about utilities almost exclusively, that purchase Wyoming coal, I do not see that one of them could qualify, and the reasons are the following.

In order to qualify as a captive shipper, they would have to meet the following four conditions. First of all, there could be no other rail lines available out of the Powder River basin. Well, there is no problem there; every single shipper could satisfy that, at least up until July 1984. Only the Burlington Northern was there.

Now, they have got to go to the second condition and satisfy that. There can be no alternative forms of transportation, such as barges. Almost every single shipper could qualify there, so that is out of the way.

Then we come to No. 3, and that says that there can be no alternative coal available to a utility. Well, many of the biggest customers of Powder River basin coal reside in the Midwest. Obviously, there is Illinois coal and Kentucky coal that would be available to them. In fact, if this were the coal that they turned to, they would be required to put scrubbers on these, almost undoubtedly, which would raise the price tremendously. So we have tremendous inefficiency. We are protecting the monopoly position of the railroad. So there is no utility that could qualify under that provision.

The fourth condition is that substitute fuels for coal could not be available. There is not a single utility which buys Wyoming coal that does not consume some other type of fuel. So there is no utility that could qualify under that provision.

So there are two conditions here which no utility could qualify under, and therefore no utility could be a "captive shipper" and could seek ICC relief. I do not think that was the purpose of the Staggers Act, and so I think the interpretation of this provision is ill-founded and misdirected. In fact, we are perpetuating the power of the monopolist in this case.

Senator DeConcini. So your answer is that under the Staggers Act, the ICC just is not apt to come to a conclusion that there is a captive shipper, certainly not in the Powder River basin?

Professor ATKINSON. Well, they have not yet ever ruled that there is a captive shipper under the provisions of the Staggers Act.

Senator DECONCINI. That was my next question. That has never occurred?

Professor ATKINSON. That has never occurred.

Senator DECONCINI. Have there been requests?

Professor ATKINSON. To my understanding, there have been. There would be no way, given the way the ICC is currently interpreting the captive shipper provision, that any shipper of Powder River basin coal would be so classified.

To me, that is one of the values of the bill that we are discussing that it would address this important issue.

Senator DECONCINI. Thank you. Dr. Andersen, in your professional opinion, would it be sufficient for the ICC to follow the legislative intent of the Staggers Act, or do you feel it is necessary to offer the guidelines?

Dr. ANDERSEN. In 1980 when the act was passed, the Consumer Energy Council felt that it was too weak. I have reviewed the evidence and it appeared that it would run into trouble.

I think it is sort of a moot question because administratively the Staggers Act has been so badly handled that there really is no protection for shippers.

I would also add to what Professor Atkinson has said that the secret contracts that are allowed now, especially for commodities in agriculture, make it very hard to prove any kind of abuse in rail transportation because there is simply no information about what rates are being charged.

The problems of protesting and the problems that the railroads have put in the way of opposition, make it virtually impossible to use the Staggers protection.

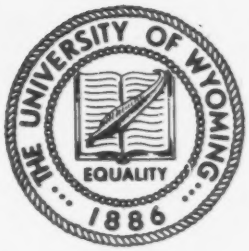
Senator DECONCINI. Gentlemen, thank you very much for your testimony, and let me ask that we might impose on you next Congress to follow up on this legislation and counsel with you in drafting what I hope will be something successful.

Mr. MCKEEVER. Thank you very much.

Dr. ANDERSEN. Thank you.

Professor ATKINSON. Thank you very much.

[Research study follows:]



FALLING WORLD OIL PRICES AND THE ROLE OF RAILROADS IN THE MARKET FOR WYOMING COAL

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PREFACE

Although some of the topics examined in this paper are technical, our hope is that it will be widely-read by both technical and lay people. Thus, we have organized the heart of the study in four major segments: background, methodology, data, and results. The organization is such that the reader can follow the analysis of a topic of interest through these four sections using our numbering system. For example, the reader interested only in the monopoly of power of railroads can begin with 2.4.1 of the background section and continue through the methodology for this topic in 3.1, the data in 4.1, and the results in 5.1. Further, the reader interested only in the results of all analysis can turn immediately to Section 5.

EXECUTIVE SUMMARY

The current market for Powder River Basin coal is substantially softer than at any time in the last decade. There are numerous examples of excess capacity and downward renegotiations of contract prices.

Among the most important factors explaining this economic downturn is the declining world oil price. In response, a competitive market would readjust delivered coal prices downward. Instead, these prices have increased dramatically since 1980, due principally to increased rail rates. This has caused further switching by utilities to other fuels which are cheaper per BTU.

This paper examines the extent and consequences of any monopoly power exercised by railroads or coal companies. If either possesses substantial monopoly power, then increased competition should significantly reduce costs and increase coal sales and severance tax collections.

We proceed to determine the degree of monopoly power exercised by railroads and coal companies. We perform accounting and financial market analysis of railroads and econometric analysis of both railroads and coal companies, obtaining the following results:

(1) based on the financial analysis:

  (a) Union Pacific is extremely healthy and risk-free; Burlington Northern does less well but is quite sound.

  (b) so called "betterment accounting" substantially biases downward their profits and rates of return;

(2) based on the econometric results:

  (a) coal companies are highly competitive producers and enjoy no significant monopoly power; Burlington Northern, in

v

particular, and Union Pacific possess substantial monopoly power;

(b) Burlington Northern's excessively high monopoly rail rates on its shipments of Powder River Basin coal are consistent with "making up" for less profitable parts of its operations. The exercise of monopoly power by Burlington Northern is particularly great for Texas utilities; monopoly profits push up rail rates as much as 16-18 percent for Houston Lighting and Power and City Public Service of San Antonio;

(c) elimination of this mark up would significantly increase sales of Powder River Basin coal by about 15 percent on average and 30 percent to Texas utilities;

(d) this would also increase Wyoming coal severance taxes by similar percentages, since the base for the taxes is mine-mouth production value, which would not change, while total coal sales would increase.

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1. INTRODUCTION

In the years 1983-4, we have witnessed a dramatic reduction in the growth of Wyoming coal sales revenues. In fact, coal production for 1983 increased from the 1982 level of 108 million tons to only 112.2 million tons. This trend could worsen if Congress mandates the retrofitting of scrubbers on existing coal-fired power plants, eliminating the option to burn compliance coal without using scrubbers, in its attempts to reduce acid precipitation. However, the Waxman bill, which would require this retrofitting, was recently defeated in committee.

At present, most Wyoming coal mines sell in a buyer's market and are operating at well below designed production capacities. The Cordero Mine in Campbell County, for example, reportedly has 24 million tons of silo capacity, but currently produces only about 10 million tons of coal per year. Some mines reportedly have renegotiated contracts at $6-$8 per ton, are probably operating at a loss, and are in production simply to retain federal leases.

This softening of the market for Wyoming coal is reflected in attitudes toward reopener clauses in production contracts. During the early phase of the coal boom, the coal companies wanted such clauses and the utility companies opposed them. Now the situation is the reverse, with utility companies demanding reopener clauses in order to take advantage of soft coal prices and the coal companies opposing them.

Many factors have significantly slowed the growth of Wyoming coal revenues. The recession, energy conservation, falling world crude oil prices, and increased world crude oil supplies have dramatically reduced the growth in sales of Wyoming coal. Under the circumstances, in a competitive market with relatively stable costs of production and

transportation, the price of Wyoming coal should also have fallen, increasing its quantity demanded. Instead, we have seen a steady growth in the delivered prices of Wyoming coal, due largely to increased rail rates, worsening its competitive position. High rail rates to distant markets (comprising up to 75 percent of delivered costs) have caused many utilities to switch from Wyoming coal to cheaper local alternatives. Utilities seek to minimize fuel costs on a BTU basis, subject to air quality regulations. In Texas, for example, many utilities have switched from Wyoming coal to local lignite, which is mostly inferior but cheaper per BTU, and currently consume approximately 30 million tons of this fuel. Assuming that Wyoming coal is produced at minimum cost and sold to utilities (which purchase 97 percent of Wyoming coal) in highly competitive markets, we argue that coal sales should be substantially increased if competition in the transportation of Wyoming coal is increased. Based on Atkinson, Kerkvliet, and Barclay (1983), there is substantial evidence that Wyoming coal is produced at minimum long-run cost and sold to utilities in highly competitive markets. Thus, coal companies cannot substantially reduce prices and stay in business. However, the two major railroads transporting Wyoming coal, the Burlington Northern and Union Pacific, appear to possess substantial monopoly power over utilities and coal producers. Thus, increased rail competition should significantly reduce rail rates and increase the demand for Wyoming coal.

By reducing rail rates, and hence, the delivered price of coal, the severance tax dollars earned by the state will also increase. Since the severance tax on coal is levied on the mine-mouth value of production, reduced rail rates will increase the quantity sold but will not alter the value of each ton which is subject to tax. Moreover, since coal

employment, income, and population will increase with coal sales, sales tax collections will increase as well.

We examine these issues in a number of steps. First, we verify and extend our preliminary results indicating that Wyoming coal is produced at minimum cost and sold in competitve markets. We also measure the extent of monopoly power exercised by the railroads and find it to be substantial. Finally, we find that the elimination of Burlington Northern's monopoly power should substantially expand the sales of Wyoming coal and coal severance taxes.

2. BACKGROUND

2.1 Definition of Terms

2.1.1 Price Elasticity of Demand

The own-price elasticity of demand for Wyoming coal is defined as

$$n_D = \frac{\%\Delta \text{ QWCD}}{\%\Delta \text{ PWC}} , \qquad (1)$$

all other variables affecting demand held constant, where %Δ QWCD = the percentage change in the quantity of Wyoming coal demanded and

%Δ PWC = the percentage change in the price of Wyoming coal.

We interpret this as a measure of the relative responsiveness of the quantity demanded to a change in its price, all else held constant. It is important to realize that n_D is validly interpreted only for small changes in price and quantity and that all the other variables affecting each utility's demand for Wyoming coal must be held constant during statistical estimation. Among these variables, are the prices of other fuels a utility might consume, kilowatt-hour output, and the sulfur content of each fuel.

The most important use of the own-price elasticity of demand is to determine a %Δ QWCD from an anticipated %Δ PWC and to estimate the

corresponding effect on total coal sales revenues. If we assume a straight line downward sloping demand curve, we can demonstrate the relationship between %Δ QWCD and %Δ PWC as well as %Δ PWC and total sales revenues (equal to PWC times QWCD). In Figure 1, we have drawn such a curve and superimposed on top of it the corresponding total sales revenue curve. If we cut the price of Wyoming coal (all else held constant) from PWC_0 = \$10 to PWC_1 = \$8 per ton and the corresponding quantity demanded increases from $QWCD_0$ = 0 to $QWCD_1$ = 2 tons per day, the %Δ PWC = $\Delta PWC/(PWC_0 + PWC_1)\cdot \frac{1}{2}$ = -2/9 and %Δ QWCD = $\Delta QWCD/(QWCD_0 + QWCD_1)\cdot \frac{1}{2}$ = 2/1. Thus, n_D = %Δ QWCD/%Δ PWC = 2/1 ÷ (-2/9) = -9. That is, a %Δ PWC = -2/9 results in a %Δ QWCD = 2. To state this somewhat differently, by cutting price by about 22 percent, coal sales are increased by 200 percent. Intuitively, total revenues should increase; this is in fact the case as indicated by the increase in the total revenue curve which is measured on the vertical axis to the right in Figure 1.

In general, if we bisect any straight line demand curve, then $|n_D| > 1$ in its upper half, $|n_D| = 1$ at its midpoint, and $|n_D| < 1$ in its lower half. We term these ranges the elastic, unitary elastic, and inelastic portions of a demand curve. Thus, price increases within the lower half ($|n| < 1$) will cause a smaller percentage decrease in quantity than price and hence an increase in total revenues. Price increases within the upper half ($|n| > 1$) will cause a greater percentage decrease in quantity than price and hence a decrease in total revenues.

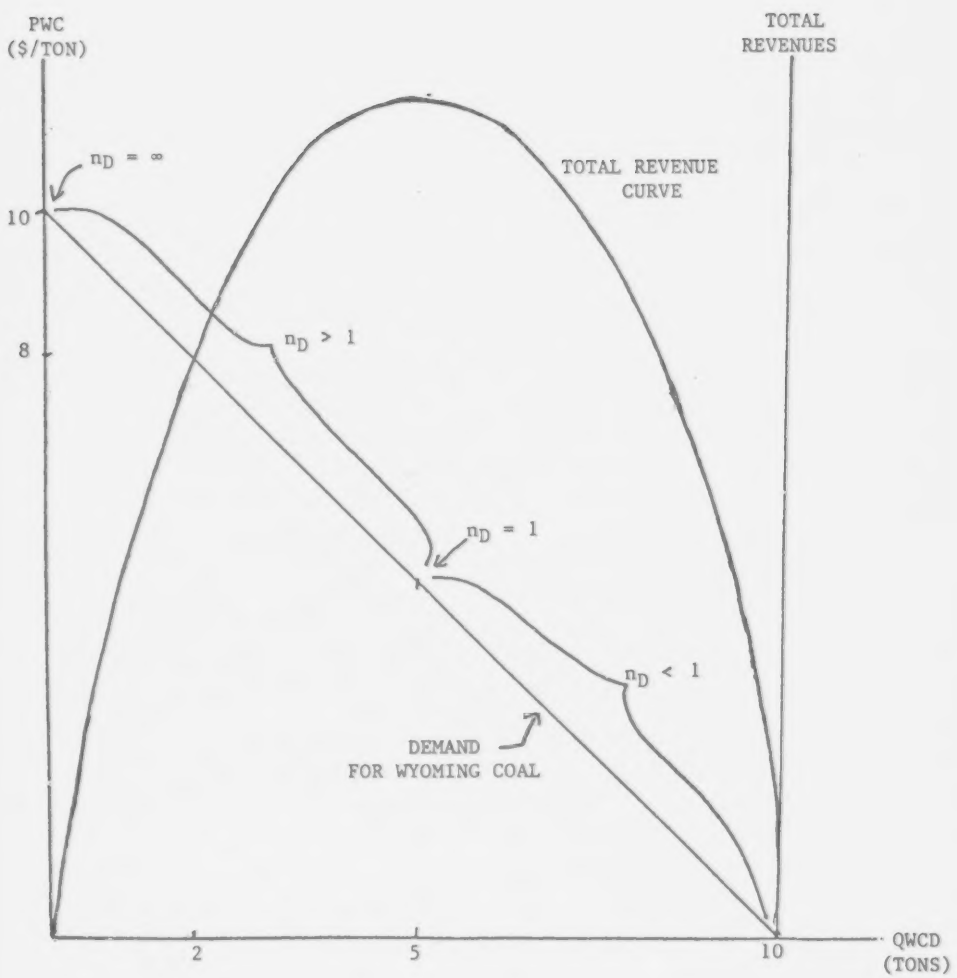
2.1.2 Monopoly Power

Since we will be constantly refering to monopoly power, it is best to

5

FIGURE 1

Elasticity of Demand



explain exactly what economic theory predicts for the behavior of the firm with monopoly power in contrast to predictions for a perfectly competitive firm. An idealized competitive firm is only a small part of an industry composed of a large number of similar firms all of which produce an identical commodity. As such, the perfectly competitive firm considers the price that will be paid for its product to be beyond its control since the product price is determined by market forces which the individual firm cannot influence. With price fixed, the firm must decide upon the amount of the product to produce which will yield the largest possible profit. The firm will obtain the largest possible profit by selling its product until the price received for the last unit of the product sold (marginal revenue) just equals the cost of making and selling the last unit (marginal cost). Note that marginal revenue is positive, zero, and negative in the elastic, unitary elastic, and inelastic portions of the demand curve, Figure 1, respectively.

This concept is illustrated in Figure 2. The costs of producing each additional unit are represented by the curve MC (Marginal Cost or Unit Cost). The price faced by the firm is P_C and this holds for any amount of the product the firm may choose to sell, so the firm's demand curve is the line P_C, which is perfectly price elastic ($n_D = \infty$). The amount of the product that yields the greatest profit is Q_C where marginal cost equals price. The firm will sell Q_C for a price of P_C per unit.

The firm with monopoly power does not find the price paid for its product to be beyond its control. The monopoly firm, in the extreme, is the only firm producing a product which has no close substitutes. So, in order to sell more of its product, the monopoly firm will have to sell each unit at a lower price. Thus, it gains revenue from selling an additional

unit but it loses revenue by selling all other units at a lower price. The net gain in revenue from selling an additional unit is called marginal revenue. The monopoly firm will maximize its profits by selling additional units until marginal revenue equals marginal cost.

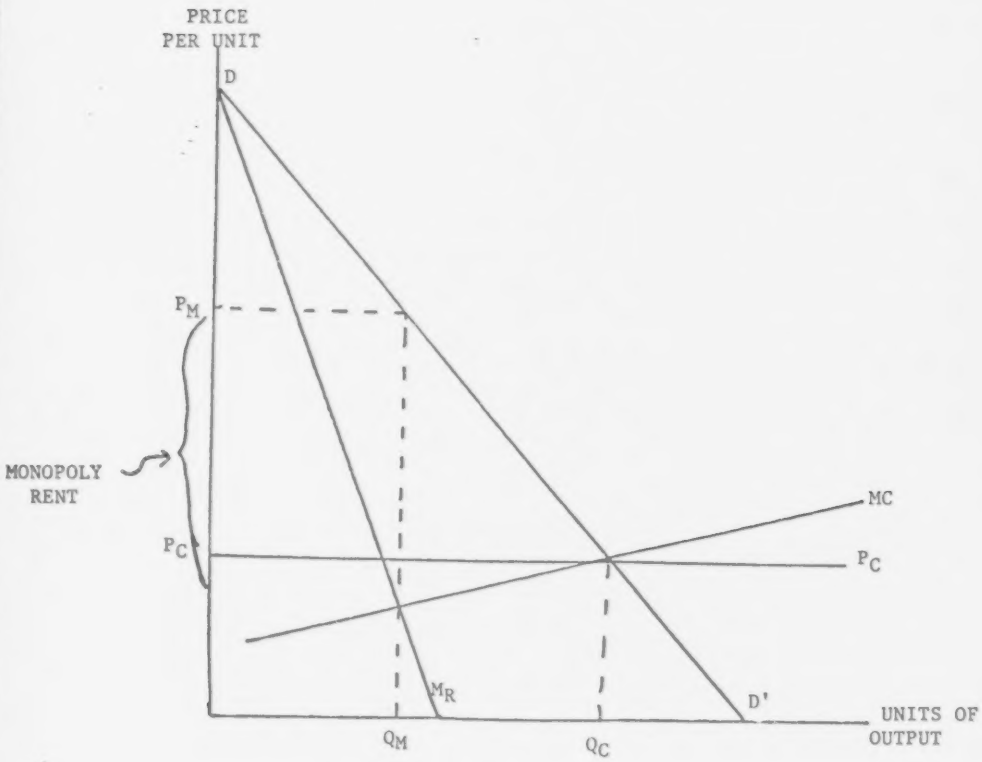
This is illustrated in Figure 2. The monopoly firm faces a demand curve labeled DD'. Its marginal revenue curve is less than the demand curve and labeled MR. The firms profit maximizing output is Q_M, determined by equating marginal revenue to marginal cost, which will be sold at price P_M per unit. A comparison of the two cases shows that a monopoly firm will produce less output and sell it at a higher price than a competitive firm with the same marginal cost. The difference betweeen the monopoly firm's marginal cost of production and the price it charges is known as excess profit per unit or monopoly rent. The goal of the monopolist is to make the demand for his product as price inelastic as possible and, hence, his monopoly rent as great as possible. However, the greater his rents, the greater the loss to society. Too little is produced at too high a price.

2.1.3 Monopsony Power

We refer to monopsony power as the ability of a single buyer of inputs to pay a price for these inputs less than the marginal or incremental valuation placed on them. An example would be a single large utility which is the sole purchaser of coal in a region. As the only buyer, the utility exercises its market power by paying less than the marginal value it places on the coal, i.e., the utility extracts monopsony rents or profits. When there are a few buyers of an input in a region, we would expect each to have some degree of monopsony power.

Figure 2

Monopoly Rent



2.2 Previous Studies of Economies of Scale, Density, and Scope for Railroads

Economists have long recognized that industries with increasing average cost will probably be competitive, whereas decreasing-cost industries are likely to be monopolistic. A decreasing cost industry is one where average and marginal costs of producing a single output fall with increasing levels of production. We term this phenomenon economies of scale or increasing returns to scale.

Most studies of railroad economies conducted in the 1950's and 1960's found few economies of scale or economies of density (where average costs fall due to a higher traffic density on a combined road, for example, after the merger of two railroads).

However, studies of railroad costs from the 1970's and 1980's tell a far different but consistent story. A number of studies indicate moderate economies of scale for railroads. Griliches (1972), using a single, aggregate measure of output (gross ton-miles) and data for 1957-61, finds no significant scale economies. Harris (1977), who criticizes Griliches for confusing economies of scale and economies of density, finds significant economies of scale and density. Keeler (1974) and Friedlander-Spady (1981) obtain largely consistent results. Economies of density are enjoyed until 7-10 million net ton-miles per route-mile, in general. Hassenkamp (1976) found increasing returns to scale as did Brown, Caves, and Christensen (1979); both additionally determined that railroads prefer to specialize in freight or passenger traffic rather than provide a combination of outputs. Thus, railroads see no reduction in costs from joint production of multiple outputs, what we refer to as economies of scope.

Table 1 indicates freight densities of major railroads in 1969 and 1980. Note the substantial increases in densities for Burlington Northern and Union Pacific. Since these railroads should be enjoying economies of density, average costs should have fallen due to increased densities. This is consistent with the existence of monopoly power for these railroads.

2.3 Allocating Fixed Costs

In determining the monopoly position of railroads hauling Wyoming coal, we must consider the railroads' specialized treatment of certain fixed cost items prior to 1983. So called "betterment" accounting practices were unique to railroads during this period (with the exception of Chicago and Northwestern which ended them in 1972). Under these rules, replacement rails, ties, and ballast on existing track were treated as current expenses. Since these expenses produce income over a considerable period of time, it has been argued that they should have been depreciated. If not, then in times of substantial replacement of these items, net profits and, hence, rates of return are artifically depressed. Comparison of rates of return of railroads with those in other industries would be misleading and typically show railroads earning far less than the market rate of return. Thus, a railroad could be earning excessive or supernormal monopoly profits, but they would go unnoticed.

Betterment accounting was ended in 1983 by the ICC. Now railroads must depreciate replacement rail, ties, and ballast over their useful lifetime. Although this varies by company and type of service, reasonable figures for the Burlington Northern and Union Pacific in Wyoming are 40, 35, and 50 years for rails, ties, and ballast, respectively. Straight line depreciating is required by law. In our analysis in section 5.1, we will

TABLE 1

Freight Densities of Major Railroads, 1969 and 1980
(Millions of net ton-miles per route-mile)

Railroad	1969	1980
Atchison, Topeka & Santa Fe	3.67	6.03
Baltimore & Ohio	5.29	4.46
Burlington Northern	2.61[a]	6.11
Chesapeake & Ohio	6.67	6.12
Chicago & Northwestern	1.63	3.10
Colorado & Southern	1.98	10.66
Denver & Rio Grande Western	4.26	5.97
Detroit, Toledo & Ironton	2.78	2.80
Fort Worth & Denver	1.10	6.55
Grand Trunk Western	3.05	3.49
Kansas City Southern	3.77	5.96
Louisville & Nashville	4.80	5.97
Marine Central	1.14	1.11
Missouri-Kansas-Texas	1.66	3.81
Missouri Pacific	2.98	5.01
Norfolk & Western	6.97	6.58[b]
Pittsburgh & Lake Erie	7.28	5.52[b]
St. Louis-Southwestern	5.74	7.75
Seaboard Coast Line	3.36	4.26
Soo Line	5.64	6.27[b]
Southern	4.22	5.35
Southern Pacific	5.64	6.27[b]
Union Pacific	4.91	7.87[b]
Western Maryland	4.11	1.80
Western Pacific	4.15	3.20

Sources: 1969 (or 1971) data, Interstate Commerce Commission, Transport Statistics (Government Printing Office, 1970, 1972); 1980 (or 1979) data, Moody's Transportation Manual (1981).

[a]First entry for Burlington Northern is 1971.

[b]Second entry for these railroads is 1979.

Taken from Keeler (1983), p. 55.

use an overall weighted average of 38.5 years, with weights derived from the 1982 expenses in each category for all railroads.

2.4 Previous Studies of Monopoly/Monopsony Power

2.4.1 Railroad Transportation

Most previous studies of coal rail rates can be placed into one of two categories, engineering studies and hedonic studies. The typical engineering study attempts to determine the cost of unit train shipments based on technological data and input prices. Technological data include the condition of the roadbed, use of single or double track lines, locomotive fuel use, etc. For an example of an engineering study, see Soo and Rieber (1975). These studies suffer from three inadequacies. First, they do not necessarily model the cost-minimizing behavior of the profit-maximizing railroad. Second, they are based on highly idealized situations and may be insensitive to actual conditions or changes in the prices of inputs. Third, while engineering studies may depict what rail rates could be, they do not depict what they will be if the railroad is able to capture monopoly rent.

Hedonic studies typically regress rail rates on various explanatory variables including ton miles, car ownership, and number of shipments annually using a variety of relationships. For example, see Lauck (1979). Like engineering studies, hedonic studies also fail to measure railroad's capture of monopoly rent. That is, from these regressions one cannot determine what part of the rate is due to the true cost of service and what part, if any, is due to railroad monopoly power.

A study that does not fall into either category is Zimmerman (1979). He explicitly considers the possibility of railroads having monopoly power

by estimating the fraction of the price differential between Western coal and natural gas, a clean higher priced alternative, which is captured by the railroads. He terms this the monopoly rent element in unit train rates. Zimmerman finds substantial evidence of higher rates for certain coal-hauling railroads. Using a sample of rates for unit-train railroad-owned cars in 1970, Zimmerman estimates that railroads capture between 6 and 38 percent of potential profits in the Midwest versus much smaller, imprecisely measured amounts in the East. He also examines data on shipments in railroad-owned cars from the Powder River Basin in 1975, excluding shipments to Colorado and Texas which were not in this sample. He finds significant evidence of increased profits of about $2.39 per ton on new shipments crossing the Mississippi River. For shipments to Chicago this represented about 25 percent of total cost, which is substantial evidence of monopoly power for the Burlington Northern. Zimmerman's model is used here but applied to Western coal rates whereas he studied mainly Midwestern and Eastern rates. In addition, we extend Zimmerman's model to include four other important elements: (1) a variable measuring whether the railroad or the utility bears the cost of providing cars for unit trains; (2) parameters to measure the rent captured by coal producers as well as railroads; (3) a variable measuring the existence of potential rent due to differences in the sulfur content of fuels; and (4) variables for alternative fuels other than natural gas, including high sulfur local coal. Our extended model is fully explained in sections 3.1 and 3.2.

2.4.2 Supply of Wyoming Coal

The most detailed recent study of the costs of producing Wyoming coal is by Atkinson, Kerkvliet, and Barclay (1983). One of the more important

results of this study was that Wyoming coal companies were producing in the range of constant returns to scale. We present a generalization of this model in section 3.2. These results regarding the competitive nature of Powder River Basin coal production are highly consistent with those in Department of Justice (1982).

2.4.3 Purchase of Western Coal by Electric Utilities

A number of studies summarized in Schmalensee (1979) have examined whether electric utilities capture rents from the sale of electricity. However, no work has been done measuring the monopsony power of these utilities vis-a-vis the railroads and coal companies. We consider this question to be beyond the scope of this paper. Western coal purchases by utility and year are shown in Table 2.

2.5 Current and Past Coal Shipping Rates

Transportation charges are a large and often major component of the final price of Wyoming coal. The percentage of the final price comprised of transportation charges in 1981 ranged from 0 in the case of nine-mouth generation to 75 percent for some distant utility operations. Most Wyoming coal is burned by utilities in either the Midwest or the Southeast, located 500 to nearly 1500 miles from Wyoming mines. Although FOB mine prices per million BTU's are lower than extraction costs elsewhere, the ability of Wyoming coal to compete with local coal or alternative fuels depends critically on low transportation rates, as discussed above.

Wyoming coal mines are served by two railroads, the Burlington Northern in the Powder River Basin and the Union Pacific in the Hanna Basin; each holds a monopoly position in its area of service (the Chicago

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TABLE 2

U.S. Electric Utilities Purchasing Western Coal: Various Years

	1973	1974	1978	1979	1980	1981
Ames, City of	x	x				
Appalachian Power	x		x			
Arkansas Power & Light					x	x
Basin Electric Power					x	x
Black Hills Power & Light	x		x	x	x	x
Cajun Electric Power					x	x
Cardinal Operating Co.			x			
Cedar Falls Utilities		x				
Central Illinois Public Service			x			
Central Louisiana Public Service						x
Commonwealth Edison, Illinois	x	x	x	x	x	x
Commonwealth Edison, Indiana	x	x	x	x	x	x
Corn Belt Power Co-op	x	x				
Dairyland Power Co-op	x	x		x	x	x
Fremont Dept. of Public Utilities	x	x				
Gulf State Utilities						x
Hastings Utilties						x
Houston Lighting & Power			x	x	x	x
Illinois Power	x	x	x	x		
Independence, City of Power & Light		x				
Indiana and Kentucky Electric	x	x	x			
Indiana and Michigan Electric	x	x	x			
Indianapolis Power & Light		x				
Interstate Power			x	x	x	x
Iowa Electric Light & Power		x				
Iowa-Illinois Gas & Electric		x				
Iowa Power & Light	x	x	x	x	x	x
Iowa Public Service	x	x	x	x	x	x
Iowa Southern Utilities	x	x	x	x	x	x
Kansas City Board of Public Utilities	x	x	x			x
Kansas City Power & Light	x	x	x	x	x	x
Kansas Power & Light		x	x	x	x	x
Lake Superior Distr. Power		x				
Lower Colorado River Utility					x	x
Madison Gas & Electric						x
Montana Dakota Utilities					x	x
Montana Power Company					x	x
Muscatine Power & Light		x				
Nebraska Power & Light	x	x	x	x	x	x
No. Indiana Public Service	x	x	x	x	x	x
No. States Power	x	x				
Ohio Electric		x	x	x		

TABLE 2 (continued)

	1973	1974	1978	1979	1980	1981
Ohio Power	x				x	x
Ohio Valley Electric Co-op		x				
Oklahoma Gas & Electric			x	x	x	x
Pacific Power & Light	x	x	x	x	x	x
Portland General Electric				x	x	x
Public Serivce Co. of Colorado	x	x	x	x	x	x
Public Service Co. of Indiana			x			
Public Service Co. of Oklahoma				x	x	x
St. Joseph Light & Power	x	x				
San Antonio, City of, Public Service			x	x	x	x
Southwestern Electric Power			x	x	x	x
Southwestern Public Service			x	x	x	x
Tennessee Valley Authority			x	x		
Union Electric		x	x	x	x	x
United Power Association					x	
Upper Pennisula Generating Company					x	x
Utah Power & Light	x	x	x	x	x	x
Virginia, Minnesota Municipal Power					x	x
Western Farmer's Electric Co-op						x
Western Illinois Power Co-op					x	
Wilmar, Minnesota Municipal Power					x	x
Winnetka, Village of			x			
Wisconsin Electric Power	x	x	x	x	x	x
Wisconsin Power & Light	x		x		x	x
Wisconsin Public Service Co-op						x

and Northwestern will soon enter the Powder River Basin). This lack of competition should allow the two railroads to earn monopoly rents by charging more than the minimum price required to cover the true costs of transporting Wyoming coal. Further, they may increase these rates to the detriment of Wyoming coal producers and consumers. Rates are determined from negotiations between individual utilities and the railroads. Differences in the ability of railroads to exercise their monopoly power plus differences in the actual cost of service and the date when the rate was established lead to wide variation in the price per ton-mile of coal charged by the railroads.

The transportation rates of interest are those involving unit train shipments in the neighborhood of 5,000 to 10,000 tons per shipment. Rates include transporation from the mine-loading facility to the utility-unloading facility but do not include the cost of loading or unloading, since they are borne by the mine and utility, respectively. Maximum loading and unloading times are usually specified. Railroad tariffs usually specify minimum annual volumes and are sometimes graduated with lower costs per ton associated with larger annual volumes, expecially for coal originating with the Union Pacific Railroad. Rates vary also with the ownership of coal-carrying cars--lower rates are offered to utilities providing cars for unit train service. Further, the number of railroads involved in a completed delivery, ranging from one to five, is directly related to the rate per ton-mile.

Tariffs for shipping Western coal have increased markedly in recent years. In the case of eight utilities for which both 1980 and 1983 tariffs are known, the average rate of increase for the three year period was 36 percent with a high of 58 percent in the case of Kansas Power and Light.

Between 1981 and 1983, known tariffs increased an average of 25 percent with a high of 60 percent in the case of Wisconsin Power and Light. This points to a continuation of the trend of large increases in tariffs since the Burlington Northern first offered low rates to encourage the use of Western coal in the 1970's.

Utilities are highly sensitive to rate increases and have made several efforts to prevent them. Examples include the San Antonio Case (ICC Docket No. 36180) and the case of Houston Power and Light (ICC Docket No. 37679). However, the Interstate Commerce Commission's interpretation of the Staggers Act of 1980 seems to have limited the ability of utilities to challenge rate increases (see Mitchell (1983)).

The study of railroad rates is complicated by the difficulty of obtaining a continuous series of rates for any one utility. The rates, listed in Table 3, indicate some of the gaps in the data. A further complication is that a substantial amount of Western coal is shipped by rail to the Mississippi River or another waterway at which point it is loaded onto barges for final delivery. The rates for barge shipment are unavailable, so that the percentage of the delivered cost attributed to all transporation services cannot be accurately determined for these coal shipments.

3. METHODOLOGY

We employed two basic techniques to measure the monopoly power of railroads. First, we examined gross rates of return for railroads and financial market valuation of assets. To the extent these appear overly healthy or super-normal when adjusted for risk, monopoly power may be prevalent. We measure risk using "beta coefficients" which specify the

TABLE 3

Western Coal Shipping Rates
Rates ($/ton)

Utility	1980	1981	1982	1983
Arkansas Power and Light		20.36		
Basin Electric Power	3.27			4.35
Cajun Electric Power				24.10
Central Illinois Public Service		22.39	24.29	
Central Louisiana Electric				26.07
Commonwealth Edison	16.06	18.26		21.36
Dairyland Co-op	15.05			19.45
Houston Lighting and Power		23.23	25.80	28.45
Iowa Power and Light		6.70		10.95
Iowa Public Service				13.43
Iowa Southern Utilities		13.26		14.73
Kansas City Power and Light	10.84			14.42
Kansas Power and Light	7.22			11.44
Lower Colorado River Authority				25.25
Minnesota Power and Light			9.28	10.76
Montana Power Company		4.25	4.20	4.25
Nebraska Public Power	5.64			
Northern States Power	11.40	11.09		
Oklahoma Gas and Electric	10.59		16.65	
Portland General Electric	15.54			20.71
Public Service Company of Colorado		7.32	8.32	
Public Service Company of Oklahoma	12.21			16.62
San Antonio City Public Service		23.52		26.47
Southwest Electric Power	16.05			21.88
Southwestern Public Service		11.66	14.03	15.51
Union Electric		17.91		25.64
Utah Power and Light				5.27
Wisconsin Electric Power				19.37
Wisconsin Power and Light		13.96		22.37
Western Farmer's Electric Co-op				22.67
Commonwealth Edison-Indiana		20.50		24.01

amount of risk in a firm's security which cannot be eliminated through portfolio diversification. Second, we carry out econometric estimation of the percentage of excess profits or monopoly rent captured by the railroads in Wyoming.

The delivered cost of coal to utilities is determined by a bargaining process between utilities, railroads, and coal mines. Each bargaining agent will have a reservation price, below or above which no agreement is reached. For mine operators and railroad management, the reserve price will be the average cost of producing their respective product or service. To agree to a lower price would result in a net loss on each unit sold. For utilities, the reserve price is the cost of burning the cheapest available alternative fuel with the same SO_2 and BTU content. To pay more than this for Western coal would unnecessarily increase the cost of producing electricity. These reserve prices set an upper and lower limit on the price that can be eventually agreed upon. Each party will attempt to gain as much additional advantage as possible, and the final outcome depends on the extent of monopoly and monopsony power.

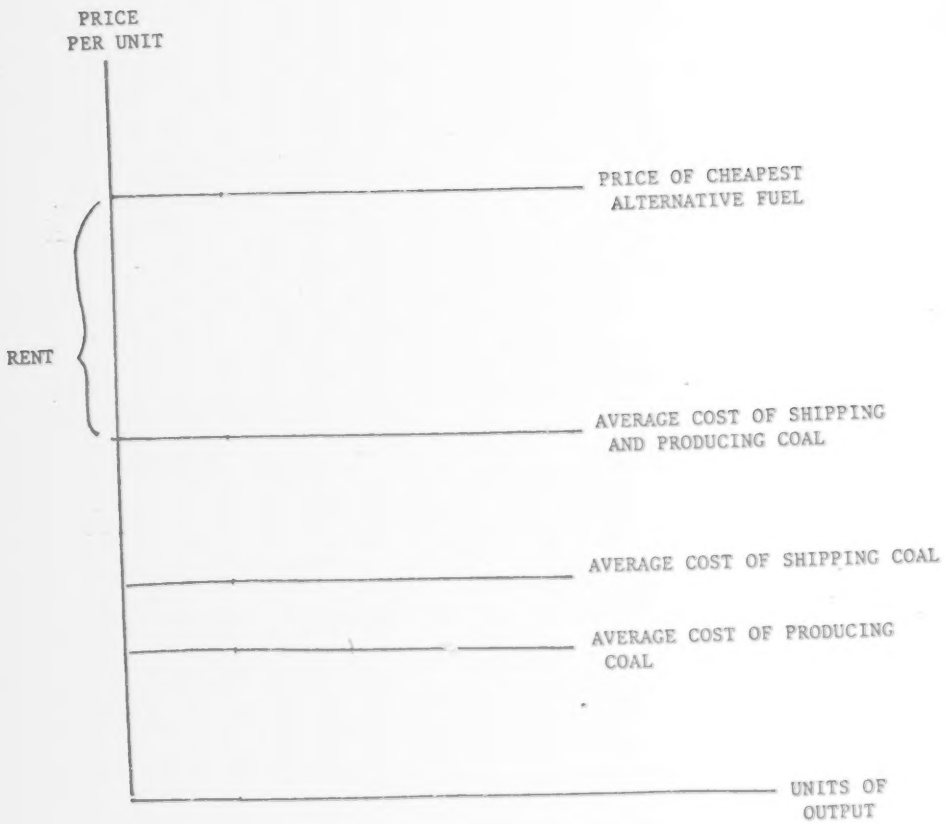
This process is illustrated in Figure 3. The minimum delivered price of coal is the average cost of shipping and producing coal and the maximum is the price of the cheapest available alternative fuel. Each party will attempt to capture as much of the available rent as possible. The following econometric models are designed to estimate the amount of rent that railroads and coal producers have actually obtained.

3.1 Estimating Monopoly Power of Railroads

The factors affecting the cost of shipping are: (1) fixed costs that do not vary with the level of service (FS); (2) "unit fixed" costs that are

Figure 3

Measurement of Rents



constant for each train used for service (dispatching costs and regular maintanence are examples) (FT); (3) variable costs that depend on the number of ton-miles shipped; and (4) car costs which are the annualized capital costs of providing the cars that comprise a unit train if railroad-owned. The true cost in cents per million BTU's hauled for typical service is as follows:

$$\hat{t}_R = \frac{TC}{MM} = \frac{\alpha_{FS}}{MM} + \alpha_{FT}\ \frac{V}{MM} + \alpha_M\ (\frac{MILES \cdot MTT \cdot V}{MM}) \qquad (2)$$

$$+ \alpha_T \cdot (\frac{Z \cdot D}{MM})$$

where

TC = total cost in cents,

MM = millions of BTU's,

V = number of trains per year required to serve the utility,

MTT = minimum tonnage per train as specified by the contract,

MILES = miles from mine to destination utility,

Z = the number of 100 car unit trains necessary to service the utility, based on mileage and an average distance of 500 miles per day covered by a unit train,

D = a binary variable (1 if railroad provides cars and 0 if utility provides cars).

This will be the reserve price of the railroad expressed in cents per million BTU's delivered. The actual tariff charges will be $\hat{t}_R$ plus the rent gained by the railroad. This tariff can be expressed as

$$t_R = \alpha_O + \hat{t}_R + \alpha_R(PALT + PALT2 - \hat{t}_R - FOBCOL) \qquad (3)$$

where

$\hat{t}_R$ = railroads' reserve price,

FOBCOL = the price paid to the Western coal producer, expressed in cents per million BTU's,

PALT = the delivered price of the cheapest availble alternative fuel, expressed in cents per million BTU's,

PALT2 = the price per million BTU's of the additional scrubbing costs which would result if the utility used dirtier local coal. PALT2 is derived following Atkinson (1983). PALT2 is zero if the alternative fuel is gas. Oil was never the alternative fuel.

The last term of equation requires some explanation. We have previously demonstrated (see Atkinson, Kerkvliet, and Barclay (1973)) that lower flue gas desulfurization costs could make Western coal a viable fuel even if its delivered costs per BTU were greater than other dirtier fuels. The additional cost that must be considered by the utility switching to an alternative fuel is embodied in PALT2. The actual tariff charge, t_R, will be average cost, $\hat{t}_R$ plus some fraction, α_R, of the difference between the alternative fuel price, including additional scrubbing costs, and the cost of Western coal. The difference is seen by the shipper as potential rent. We expect α_R to range between zero (no potential rent captured) and one (all potential rent captured). By substituting equation (2) into (3) we obtain our equation for estimation.

3.2 Estimating Monopoly Power of Coal Companies

Based on previous work, the total cost of producing coal depends mainly on the amount of coal produced. The true cost per unit of output, expressed in cents per million BTU's, for a typical Powder River Basin coal

mine is

$$\hat{t}_M = \frac{TC_M}{MM} = \frac{\alpha}{MM} + \alpha_V \frac{QWC}{MM} + \alpha_{VV} \frac{(QWC)^2}{MM} \qquad (4)$$

where

TC_M = total mining cost in cents,

MM = millions of BTU's,

QWC = number of tons of coal sold to the utility.

The reserve price of the coal producer will be the true cost of production, $\hat{t}_M$, but the actual price negotiated will be $\hat{t}_M$ plus the rent gained by the coal producer. This price can be expressed as

$$t_M = \alpha_0 + \hat{t}_M + \alpha_M(PALT + PALT2 - \hat{t}_M - TFOB) \qquad (5)$$

where

TFOB = the actual price charged by the shipper expressed in cents per million BTU's.

This equation states that the actual FOB price for coal will be the producer's reserve price, $\hat{t}_M$, plus some fraction α_M, of the difference between the alternative fuel price, including additional scrubbing costs, and the true cost of producing coal plus the shipper's charges for delivering coal, TFOB. We expect α_M to exhibit the same bounds as α_R, with the same interpretation.

4. DATA

4.1 - 4.2 Estimating the Monopoly Power of Railroads and Coal Companies

To determine the financial status of railroads, we obtained book value accounting data from Interstate Commerce Commission Transporation Statistics, Part 1: Railroads, various years. Data on the market valuation of railroad's assets comes from Value Line, 1982.

The data used for estimating railroad and coal producer's monopoly power included prices, tonnage, BTU content, and SO_2 content of fuels delivered to Western coal-using utilities for 1980 and 1981. This information was obtained from Department of Energy (1980-81). Railroad tariff data was obtained from Coal Outlook (1981-83) which provided a partial list of existing unit train rates including costs per ton of shipping, minimum annual tonnage, and other terms of service. In the few cases where the rate for only one year was available, an increase of 10 percent per year was used to obtain the second year. The alternative fuel was determined on the basis of average cost of fuels delivered to the utility's generating facilities. In most cases, other local coal was the available alternative fuel.

The availability of data limited the sample size to 73 producer-railroad-utility transactions with 30 utilities represented. The sample well represents all aspects of Western steam-coal use except for mine-mouth generating facilities.

5. RESULTS

5.1 The Monopoly Power of Railroads

We first examine the importance of betterment accounting practices for railroads by recomputing gross rates of return and then examine the degree of riskiness for each railroad. We find that the recomputed gross rates of return for the Burlington Northern and Union Pacific increase dramatically; they are among the most profitable of all railroads. Further, these two firms are considered relatively risk free and the financial market valuation of their assets is excellent. Thus, we conclude that the strong possibility of monopoly power exists for these railroads. In the second

part of this section, we examine the econometric results measuring monopoloy power.

We begin this analysis by gathering data needed to compute the gross rate of return based on book value using betterment accounting practices for each railroad. The variables, their symbol, the corresponding ICC account number, and the formula for gross rate of return are given in Table 4 for pre-1980. Table 5 contains the same information for 1982 after accounts were redefined. Table 6 presents the 1982 data required in Table 5 for the Burlington Northern, Union Pacific, Illinois Central Gulf, Chesapeake and Ohio, and Western Pacific. While the first two railroads serve Wyoming, and hence are of primary interest, the others provide wide diversity in both service region and financial viability, and serve as a basis for comparison. In Table 7, computed gross rates of return based on betterment accounting are provided. Note that while Burlington Northern, Union Pacific, and Chesapeake and Ohio appear healthy, Illinois Central Gulf and Western Pacific incur substantial losses.

We now recompute the gross rate of return based on book value for the same set of firms, replacing betterment accounting with straight-line depreciation of replacement rails, ties, and ballast for 1982 over 38.5 years. Thus, we add the value of replacement expense for rails, ties, and ballast to the numerator of r_g (since this should not have been subtracted in the first place) plus .026 times this value for depreciation. We also add the value of rails, ties, and ballast to the denominator of r_g (since this now is part of assets) and subtract .026 times this amount for depreciation. The new formula for gross rate of return and its computed values for the same set of firms are given in Table 8.

Due simply to eliminating betterment accounting in 1982, the

TABLE 4

Railroad Accounts: Variables for Computing Rates of Return Based on Book Values Using Betterment Accounting - Used by Keeler pre-1980[a]

Variable	Symbol	ICC Account Number
Net railway operating income (net of taxes and expenses)	Y	111
Federal income taxes	T	105
Taxes other than federal	T_L	110
Income from lease of road & equipment	L_I	135
Rent from leased road & equipment	L_R	157
Road property depreciation	D_P	298
Equipment depreciation	D_F	336
Current assets	A_C	14
Current liabilities	L_C	55
Total road & equipment property	RE	23
Improvements on all leased property	IL	32

Gross rate of return, r_g, is computed as

$$\frac{Y + T + T_L + L_I - L_R + D_P + D_E}{A_C - L_C + RE + IL}$$

[a]From Interstate Commerce Commission, Transporation Statistics, Part 1: Railroads (Government Printing Office, pre-1980).

TABLE 5

Railroad Accounts: Variables for Computing Rates of Return Based on Book Values Using Betterment Accounting - 1982[a]

Variable	Symbol	ICC Account Number
Net revenue from railway operations (net of expenses)	NR	115
Income from lease of road & equipment	L_I	167
Rent for leased roads & equipment	L_R	168
Way and structure depreciation	D_{WS}	525
Equipment depreciation	D_E	583
Current assets	A_C	14
Current liabilities	L_C	40
Total road & equipment property	RE	24, 25
Unallocated items - property	UP	26

Gross rate of return, r_g, is computed as

$$\frac{NR + L_I - L_R + D_{WS} + D_E}{A_C - L_C + RE + UP}$$

[a]From Interstate Commerce Commission, Transportation Statistics, Part 1: Railroads (Government Printing Office, 1982).

TABLE 6

Data to Compute Rates of Return Based on Book Value Using Betterment Accounting, Various Railroads, 1982
(thousands of dollars)

ICC Account Number	Railroad				
	Burlington Northern	Union Pacific	Illinois Central Gulf	Chesapeake and Ohio	Western Pacific
115	240,956	168,968	-88,242	101,095	-11,320
167	11	125	36	0	0
168	50	464	684	289	v
525	25,731	13,143	7,331	7,824	484
583	72,473	97,000	25,924	12,852	7,109
14	1,259,847	476,367	169,040	348,321	75,942
40	1,008,939	393,219	248,639	289,692	59,132
24, 25	5,136,709	3,728,974	1,489,056	1,675,803	120,950
26	15,532	4,532	74,545	12,445	0

TABLE 7

Gross Rate of Return on Investment of Major Railroads Based on Book Value Using Betterment Accounting, Various Railroads, 1976-9, 1982

Railroad	r_g 1976-79	r_g 1982
Burlington Northern	5.1	6.3
Union Pacific	10.8	7.3
Illinois Central Gulf	2.5	-3.8
Chesapeake and Ohio	4.7	7.0
Western Pacific	6.7	-2.7

Gross rate of return, r_g, computed as

$$\frac{NR + L_I - L_R + D_{WS} + D_E}{A_C - L_C + RE + UP}$$

TABLE 8

Gross Rate of Return on Investment of Major Railroads Based on Book Value with Rails, Ties & Ballast Replacement Depreciated over 38.5 years (straight line), 1982, and Percent Charge Relative to Betterment Accounting

Railroad	r_g	%Δ
Burlington Northern	8.8	39.7
Union Pacific	8.0	9.6
Illinois Central Gulf	-.01	99.7
Chesapeake and Ohio	8.5	21.4
Western Pacific	.67	124.8

Gross rate of return, r_g, computed as

$$\frac{NR + L_I - L_R + D_{WS} + D_E + RE_{RTB} + .026 \cdot RE_{RTB}}{A_C - L_C + RE + UP + RE_{RTB} - .026 \cdot RE_{RTB}}$$

where

RE_{RTB} = replacement expenses for rails, ties, and ballast
D_{RTB} = depreciation for rails, ties, and ballast assuming straight line rate of .026

percentage increases in gross rates of return are enormous. For Burlington Northern, the percent increase is 39.7; for Union Pacific, 9.6; for Illinois Central Gulf, 99.7; for Chesapeake and Ohio, 21.4; and for Western Pacific, 124.8. Net income before depreciation and taxes increase substantially also--43 percent for Burlington Northern. Clearly, Burlington Northern and Union Pacific are quite healthy financially and among the most healthy of all railroads in the U.S. as seen from Table 9.

Using data from Value Line, we also examine the current financial market valuation of rail assets in Table 10. The financial position of Union Pacific is outstanding. Value Line, May 22, 1981 states that its profits are excellent. Union Pacific's valuation ratio, defined as recent price per share to book value, is substantially greater than one. A value of one indicates a normal or competitive rate of return. A value in excess of one is consistent with monopoly profits. A high valuation ratio also exists for Chicago Northwestern. Even though Burlington Northern's financial valuation is not as optimistic, its valuation ratio is still .82.

The corrected gross rates of return are below the historical average of 15-16 percent for all U.S. non-financial corporations. However, this should not be interpreted as evidence against the exercise of monopoloy power by Burlington Northern in the Powder River Basin. First, the Union Pacific and Burlington Northern are relatively riskless, with beta coefficients very close to one, the market average. Secondly, Burlington Northern is a massive rail company, with some unprofitable routes and substantial sunk costs which should be written off. Monopoly power may exist in the Powder River Basin but not be reflected in data on gross rates of return for all operations.

Turning now to the econometric estimates using the methodology

TABLE 9

Percent Returns on Investment of Major Railroads, 1946-79

Railroad	1946-50	1951-55	1956-60	1961-65	1966-70	1971-75	1976-79
Atchison, Topeka & Santa Fe	8.8	9.6	7.7	6.7	6.1	6.8	7.1
Baltimore & Ohio	6.6	7.3	5.6	4.4	5.5	7.0	8.2
Burlington Northern (Great Northern)	7.0	7.9	6.7	6.0	5.1	4.6	5.1
Chesapeake & Ohio	9.2	10.5	9.7	7.3	6.6	7.1	4.7
Chicago, Burlington & Quincy	8.9	8.2	5.7	5.3	4.8[a]	---	---
Chicago, Milwaukee St. Paul & Pacific	4.3	4.3	3.9	4.3	3.4	2.3	-4.9
Chicago & Northwest.	3.6	3.3	2.9	4.1	3.0	7.0	6.7
Chicago, Rock Island & Pacific	7.0	7.0	4.9	4.0	1.6	-2.0	-2.0[a]
Cincinnati, New Orlean & Texas Pacific	14.3	17.8	12.0	6.8	9.2	12.8	17.6
Conrail							
New York Central	4.4	5.9	5.2	4.4	4.3[a]	---	---
Pennsylvania	4.0	5.9	4.8	4.7	1.8	-1.3	-22.7
Denver & Rio Grande Western	6.4	10.8	10.8	9.7	9.8	10.2	10.8
Florida East Coast	3.2	4.3	4.0	4.0	3.7	9.6	8.6
Gulf, Mobile & Ohio	7.1	8.9	5.4	5.2	6.3	4.5[a]	---
Illinois Cntrl. Gulf	10.8	9.7	6.4	5.3	5.2	5.0[a]	2.5
Louisville & Nashville	7.5	9.5	6.8	6.1	6.2	6.7	6.2
Missouri Pacific	5.9	6.0	6.4	6.4	5.9	6.8	9.4
New York, New Haven & Hartford	3.8	4.2	1.7	-0.9	-1.6[a]	---	---
Norfolk & Western	9.9	10.6	10.6	11.1	8.8	9.0	10.8
Northern Pacific	5.4	5.0	4.5	3.8	3.9[a]	---	---
Pittsburgh & L. Erie	12.2	13.0	9.4	10.3	9.6	7.7	11.3
Richmond, Fredericksburg & Potomac	10.3	13.0	11.9	10.4	12.2	13.6	13.2[a]
St. Louis-San Fran.	5.9	7.5	5.5	5.9	6.9	6.3	7.4
Seaboard Coast Line (Seaboard)	6.6	9.5	7.5	6.7	5.7	5.9	7.8
Seaboard Coast Line (Atlantic Coast)	4.0	5.5	4.6	5.8	6.2[a]	---	---
Soo Line	3.8	4.0	3.8	4.8	5.7	8.3	10.7
Southern	7.4	10.8	9.8	9.1	9.3	9.0	9.2
Southern Pacific	7.8	7.9	5.6	6.4	6.8	6.9	5.8
Union Pacific	7.6	8.1	7.8	7.8	8.0	9.6	10.8
Western Pacific	6.3	8.5	6.1	6.6	3.9	4.7	6.7

[a]Average for portion of period during which the railroad operated.
Taken from Keeler (1983), p. 9.

TABLE 10

Financial Market Valuation of Rail Assets, 1981

Railraod	Financial Strength	Pre-tax Profit Margin	Percent Price ($/share)	Book Value ($/share)	Valuation Ratio	Beta Coefficient
Burlington Northern[a]	B+	6.5%	59.00	71.95	.82	1.25
Union Pacific[a]	A+	14.%	58.00	32.35	1.79	1.15
Chicago and Northwestern[b]	C++	---	66.00	38.20	1.73	1.50

[a] Value Line, May 22, 1981.
[b] Value Line, April 10, 1981.

outlined in 3.1 above, we estimated the following equation to determine the railroad's monopoly power:

$$t_R = \underset{(6.44)*}{60.2272} - \underset{(.56 \cdot 10^8)*}{.1404 \cdot 10^9} \cdot \left(\frac{1}{MM}\right) - \underset{(565 \cdot 10^3)*}{.2020 \cdot 10^9} \cdot \left(\frac{V}{MM}\right)$$

$$+ \underset{(.134)*}{.498} \cdot \left(\frac{MILES \cdot MTT \cdot V}{MM}\right) + \underset{(.11 \cdot 10^9)}{.77 \cdot 10^8} \cdot \left(\frac{Z \cdot D}{MM}\right) \qquad (6)$$

$$+ \underset{(.40)*}{.072} (PALT + PALT2 - \hat{t}_R - FOBCOL)$$

The variables are defined in 3.1. Standard errors are given in parentheses and asterisks indicate significance at the .05 level. These results can be interpreted as follows: Using the sample mean of 48,000,000 total BTU's delivered, the cost to the utility of the railroad providing unit train cars is about 1.6 cents per million BTU's, or an annual cost of about $770,000. The coefficient on MILES · MTT · V/MM indicates increasing returns to scale, which is consistent with monopoly power.

The parameter of interest is the rent seeking parameter, α_R, which is estimated to be .072 and is significant at the .05 level. Based on this evidence, we can conclude with a high level of confidence that railroad rates for this sample do not consist only of true costs that must be recovered if the railroad is to stay in business. Rather the rates also contain an element of monopoly rent. Interpreting α_R as a fraction, we estimate that the railroads are collecting 7.2 percent of the potential rents with the remainder collected by the utility and coal companies, or passed on to the electricity consumer. This percentage is substantial and even larger percentages are indicated for certain utilities with few available alternatives. It should also be recalled that our sample data do not include rates for 1982 to the present and, therefore, our estimates do

not account for most of the major rate increases that have occurred in the less regulated environment of the post-Staggers Act years.

It is interesting to compare these percentages for some of the largest consumers of Powder River Basin coal. Table 11 presents the percentage of potential rents which are captured by the Burlington Northern (BN) and Union Pacific (UP) railroads on coal shipments to 36 utilities in 1981. The letters W and M after each utility name indicate that coal shipments originated in Wyoming and Montana, respectively. We expect that these utilities should be able to exercise some degree of monopsony power to reduce the rents captured by the railroads. This rent reduction should increase with the size of the utility and availability of cost competitive substitute fuels which meet air quality requirements.

The results confirm this expectation. With Commonwealth Edison, which has many fuel alternatives and is one of the largest consumers of Powder River Basin coal, Burlington Northern captures only about one percent of possible rents. Another large consumer of Powder River Basin coal, Houston Lighting and Power, fares less well; Burlington Northern extracts about 14 percent of potential rents. The monopsony power of this utility appears to be outweighed by its reliance on low-sulfur Powder River Basin coal. Burlington Northern extracts almost 18 percent of the available rents from City Public Service of San Antonio. This utility is smaller than Houston Lighting and Power and presumably exercises less monopsony power. Finally, Burlington Northern extracts about 16 percent of potential rents from Arkansas Power and Light. The 1983 reduction of 5-8 percent in Burlington Northern's rail rates to this utility, due to the threat of a coal slurry pipeline, is consistent with a negotiated settlement which reduced the extracted rent by about one half, i.e., "split the difference".

TABLE 11

Percentage of Potential Rents Captured
By Railroads, 1981

Railroad	Utility	Percentage of Rents Captured (as decimal)
BN	Arkansas Power & Light-W	.156093
BN	Central Illinois Light-W	.158646
BN	Commonwealth Edison-W	.102295E-01
BN	Commonwealth Edison-M	.140026E-01
BN	Dairyland Co-op-W	.759684E-01
BN	Dairyland Co-op-M	.687658E-01
BN	Houston Power & Light-W	.151662
BN	Houston Power & Light-M	.134027
BN	Iowa Power & Light-W	.950334E-01
BN	Iowa Public Service-W	.886106E-01
BN	Iowa Southern Utilities-W	.845351E-01
BN	Kansas City Power & Light-W	.769512E-01
BN	Kansas Power & Light-W	.108019
BN	Lake Superior Dist. Power-M	.329617E-01
BN	Lower Colorado River Authority-W	.156665
BN	Lower Colorado River Authority-M	.138695
BN	Minnesota Power & Light-M	.230403
BN	Nebraska Public Power-W	.175435
UP	No. Indiana Public Service-W	.134849E-01
BN	No. States Power-M	.910161E-01
BN	Oklahoma Gas and Electric-W	.104930
UP	Omaha Public Power Distr.-W	.211846
BN	Portland General Electric-W	.271280
BN	Public Service Co. of Colorado-W	.632743E-01
BN	Public Service Co. of Oklahoma-W	.646192E-01
BN	City Public Service-San Antonio-W	.175447
BN	Southwestern Electric Power-W	.782178E-01
BN	Southwestern Public Service-W	.144560
BN	Union Electric-W	.673616E-01
BN	Wisconsin Electric Power-W	.579488E-01
BN	Wisconsin Power & Light-W	.504004E-01
BN	Wisconsin Power & Light-M	.808364E-01
BN	Commonwealth Edison-Indiana-W	.113847
BN	Commonwealth Edison-Indiana-M	.125690

5.2 The Monopoly Power of Coal Companies

We now examine whether coal producers capture a significant portion of availabe rents. Using the methodology outlined in section 3.2 above, we estimated the

following equation for coal producer prices:

$$t_M = \underset{(54.9)^*}{478.1} + \underset{(.14 \cdot 10^8)}{.13 \cdot 10^8} \cdot \left(\frac{1}{MM}\right) - \underset{(.10 \cdot 10^7)^*}{.76 \cdot 10^7} \cdot \left(\frac{QWC}{MM}\right) + \underset{(27.5)}{1.08} \cdot \left(\frac{QWC^2}{MM}\right) + \underset{(.04)}{.05} \cdot (PALT + PALT2 - \hat{t}_M - TFOB) \quad (7)$$

The variables are defined in section 3.2. Standard errors are given in parentheses and asterisks indicate significance at the .05 level. The results indicate approximately constant returns to scale in coal production.

The rent seeking parameter, α_M, is estimated to be .05. While positive, as expected, α_M is small and not significant even at the .10 level. We can, therefore, conclude with a high level of confidence that coal producers do not capture rent from coal sales either because of fuel-price or sulfur-content differences. This result is consistent with our prior expectations that coal producers lack monopoly power.

These econometric results are consistent with the perceived wisdom regarding Burlington Northern. Although it is a healthy railroad, it is not regarded by the market to be as financially sound as some, particularly Union Pacific. Some of Burlington Northern's wide network of track is not profitable or earns less than the market rate of return. To compensate for this, Burlington Northern apparently exercises substantial monopoly power over many of its coal customers served from the Powder River Basin.

What would be the effect on coal sales and Wyoming severance tax

revenues if Burlington Northern's monopoly power were eliminated? Assuming coal companies remain competitive, rail rates and the delivered price of coal should fall by about 8 percent overall. Assuming further that the overall own-price elasticity of demand for Wyoming coal is about -1.85 (see Atkinson, Kerkvliet, and Barclay (1983)), this price reduction would cause an approximate 15 percent increase in coal sales (given perfectly elastic or horizontal coal supply as estimated in section 5.2). This would also produce approximately a 15 percent increase in coal severance taxes. Severance taxes are levied on the mine-mouth value of production, which is independent of changes in transportation rates. Thus, a lower delivered price will increase sales by 15 percent, with no reduction in mine-mouth value. For Texas utilities, these figures would approximately double. The overall result for Wyoming due to an 8 percent reduction in Burlington Northern's rates would be extremely beneficial.

6. CONCLUSION

The current market for Powder River Basin coal is substantially softer than at any time in the last decade. There are numerous examples of excess capacity and downward renegotiations of contract prices.

Among the most important factors explaining this economic downturn is the declining world oil price. In response, a competitive market would readjust delivered coal prices downward. Instead, these prices have increased dramatically since 1980, due principally to increased rail rates. This has caused further switching by utilities to other fuels which are cheaper per BTU.

This paper examines the extent and consequences of any monopoly power exercised by railroads or coal companies. If either possesses substantial

monopoly power, then increased competition should significantly reduce costs and increase coal sales and severance tax collections.

We proceed to determine the degree of monopoly power exercised by railroads and coal companies. We perform accounting and financial market analysis of railroads and econometric analysis of both railroads and coal companies, obtaining the following results:

(1) based on the financial analysis:

(a) Union Pacific is extremely healthy and risk-free; Burlington Northern does less well but is quite sound.

(b) so called "betterment accounting" substantially biases downward their profits and rates of return;

(2) based on the econometric results:

(a) coal companies are highly competitive producers and enjoy no significant monopoly power; Burlington Northern, in particular, and Union Pacific possess substantial monopoly power;

(b) Burlington Northern's excessively high monopoly rail rates on its shipments of Powder River Basin coal are consistent with "making up" for less profitable parts of its operations. The exercise of monopoly power by Burlington Northern is particularly great for Texas utilities; monopoly profits push up rail rates as much as 16-18 percent for Houston Lighting and Power and City Public Service of San Antonio;

(c) elimination of this mark up would significantly increase sales of Powder River Basin coal by about 15 percent on average and 30 percent to Texas utilities;

(d) this would also increase Wyoming coal severance taxes by similar percentages, since the base for the taxes is mine-mouth production value, which would not change, while total coal sales would increase.

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Senator DECONCINI. Our next panel will be Judi L'Italien, manager, traffic, Mobil Chemical Co.; Darrell Wallace, director of transportation, Union Equity Cooperative Exchange; and William C. Harding, vice president of transportation, Louis Dreyfus Corp.

Ms. L'Italien, please proceed. Your full statements will be in the record and, as indicated by the chairman, we have a 5-minute rule so we can get through all the witnesses today.

STATEMENT OF A PANEL CONSISTING OF: JUDI L'ITALIEN, MANAGER, TRAFFIC, MOBIL CHEMICAL CO., RICHMOND, VA, ON BEHALF OF THE FERTILIZER INSTITUTE; DARRELL R. WALLACE, DIRECTOR OF TRANSPORTATION, UNION EQUITY COOPERATIVE EXCHANGE, ENID, OK, ON BEHALF OF THE NATIONAL COUNCIL OF FARMER COOPERATIVES; AND WILLIAM C. HARDING, VICE PRESIDENT OF TRANSPORTATION, LOUIS DREYFUS CORP., STAMFORD, CT, ON BEHALF OF THE NATIONAL GRAIN & FEED ASSOCIATION

Ms. L'ITALIEN. Mr. Chairman, my name is Judi L'Italien and I am manager of traffic for Mobil Chemical Co., Chemical Products Division. I appear here today on behalf of the Fertilizer Institute, on which I am a member of the steering committee of the transportation committee.

The institute represents over 320 members, including producers, manufacturers and traders, retail dealers and distributors of fertilizer and fertilizer materials. Its members are major shippers and receivers and retailers of fertilizer and fertilizer materials, and a vital link in America's agricultural food chain.

On behalf of the membership of the institute, we wish to thank this committee for the opportunity to present our industry's views on S. 2417. We wholeheartedly support passage of this bill and we believe that creating access to singularly controlled railroad facilities is the most practical means for restoring competition within the railroad industry.

America's farmers and other shippers of agricultural products are heavily dependent upon the railroad industry for their transportation needs. Loss of competitive alternatives results in passing along these transportation costs to the consuming public, if possible, or accepting their losses and hoping to stay in business.

Unfortunately, railroad competition has declined dramatically over the past 5 to 6 years. This jeopardizes the ability of the agricultural community to economically ship its goods.

To begin with, there has been a steady stream of merger activity which significantly has reduced the number of carriers to a relative handful of giants, each of which is dominant in its own region—the Union Pacific system, the Burlington Northern system, the CSX Corp., the Norfolk Southern, and soon the Santa Fe Southern Pacific.

Coupled with these mergers, we have been faced with a recent flurry of activity to cancel joint rates and reciprocal switching. This has not only reduced competition, but it has limited our choices.

In the past, reciprocal switching arrangements were used to create competition where a particular origin or destination or plant

would otherwise be served by only one carrier. Joint rates afforded the shipper an opportunity to choose one carrier or routing over another, and frequently this could be accomplished without suffering any type of rate penalty.

However, beginning around 1982 and continuing into the present day, many of the Nation's largest carriers have been canceling joint rates and restricting or canceling reciprocal switching agreements where the carrier has been able to set himself up in a position where he can perform the total service.

The Interstate Commerce Commission has thus far taken no steps to stop these new railroad practices. Now, many agricultural shippers find that they must deal with only one carrier rather than rail carriers which compete for their traffic.

The shipper has no ability to take its business elsewhere when there is nowhere else that they can do business. At the same time, the Interstate Commerce Commission has made it virtually impossible for a shipper to obtain relief from this rebirth of rail monopoly power.

The Commission, for example, has proposed rules that would expand ratemaking freedom to the same level at which it would cost a shipper to duplicate existing railroad facilities—a solution found impractical by the Supreme Court more than 70 years ago.

We have now almost come full circle and shippers are coming to recognize that the ICC no longer can be relied upon to protect the public from anticompetitive railroad conduct, nor to protect the captive shipper from excessive transportation expense.

However, the gains from deregulation should not be overlooked and, as such, we now need to look at the obvious alternative relief under the country's antitrust laws. As presently structured, however, these laws make it difficult to face the railroads successfully on an antitrust issue.

To begin with, there are serious questions regarding the ICC's primary jurisdiction. Further, the problems of proving the existence of anticompetitive conspiracies or of defining relevant markets are major obstacles to effective antitrust relief for shippers tied to the services of a single carrier.

For these reasons, TFI supports passage of S. 2417, for without reverting to public utility-style regulation, the bill, we believe, would free those shippers monopolized by a single carrier by requiring that railroad to allow competitors access over its tracks.

We note that the Federal courts in antitrust actions have long ordered competitors access to essential facilities of a monopolist where such was needed to ensure competition. Further, a grant of trackage rights has in the past been employed as a condition for mergers.

Nevertheless, we believe that trackage rights as a merger condition alone would not necessarily restore competition. A carrier may or may not have the desire to serve a particular shipper, dependent upon a variety of economic and operational factors.

However, the shipper may nonetheless have the desire to use the carrier, and therefore we support this bill's recognition of the importance of direct shipper access to a competing rail carrier or to the shipment's destination.

In closing, I reiterate that there have been beneficial results of deregulatory freedoms gained by the railroad industry, but there has been a wholesale loss of competitive options with increasing monopoly power.

Railroads have wanted to do business in a nonregulated environment and, as such, this bill is a reasonable followthrough to the deregulation that the railroads now enjoy. Passage is needed to restore competition.

Thank you.

[The prepared statement follows:]

43-746 O - 85 - 4

STATEMENT OF
JUDI L'ITALIEN, MOBIL CHEMICAL COMPANY
ON BEHALF OF
THE FERTILIZER INSTITUTE
IN SUPPORT OF S.2417,
THE CONSUMER RAILROAD TRANSPORTATION ANTIMONOPOLY ACT

Summary

The Fertilizer Institute (TFI) is a voluntary, non-profit association whose members represent approximately 95% of domestic fertilizer production in the United States.[1/] In partnership with our Nation's farmers, TFI's members contribute to our abundant supply of food and fiber.

TFI submits this statement in support of S.2417 for the following reasons:

(1) Most shippers of agricultural and farm products are dependent on rail transportation.

(2) The last several years have seen a steady decrease of intra-rail competition due to systematic railroad merger activity and wholesale railroad cancellation of joint rate and reciprocal switching arrangements, resulting in a rebirth of rail monopoly power.

(3) The Interstate Commerce Commission has failed to properly use its authority to prohibit the growth of unlawful railroad monopoly power.

(4) The present structure of the antitrust laws do not provide feasible protection to the public from the ICC's failure to properly exercise its authority.

1/ TFI represents over 320 members, including producers, manufacturers, traders, retail dealers and distributors of fertilizer and fertilizer materials. Its members are major shippers, receivers and retailers of fertilizer and fertilizer materials, and a vital link in America's agricultural food chain.

(5) Amending the antitrust laws, by mandating access to closed facilities, is the most practical means of restoring competition and prohibiting unlawful railroad monopoly.

The Nation's antitrust laws were designed with one basic goal: the maintenance and preservation of competition in the marketplace.[2/] This country's shippers of agricultural and farming products are especially sensitive to the importance of competitive alternatives for transportation services. These shippers are heavily dependent on the railroad industry for their transportation needs. Thus, the existence of as many alternate rail carriers as possible is essential if the Nation's agricultural and farm products are to move efficiently and economically. If America's agri-businesses lose competitive transportation alternatives, they will be forced either to pay higher rates or not move their products at all. The latter alternative is, of course, unacceptable; but if agricultural shippers must pay the higher rates, those costs either must be absorbed or passed on to the consuming public.

Unfortunately, the last several years have seen a steady diminution of competition among rail carriers. Most obvious has been the string of ICC-approved mergers between some of the largest carriers. For example, the Atlantic Coast Line

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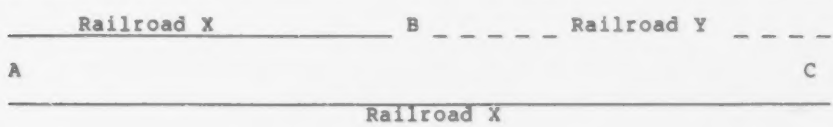
2/ See, generally United States v. Von's Grocery Co., 384 U.S. 270, 275 (1966); Northern Pacific R. Co. v. United States, 356 U.S. 1, 4 (1958); United States v. Aluminum Co. of America, 148 F.2d 416, 427 (2d Cir. 1945).

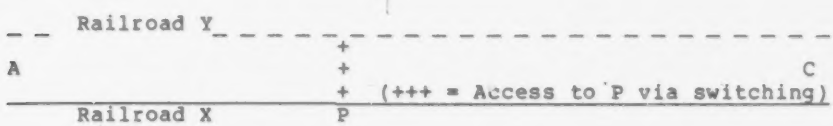
merged with the Seaboard Line to form the Seaboard Coast Line, the Seaboard and the Louisville & Nashville merged to form the Family Lines, the Baltimore & Ohio merged with the Chesapeake & Ohio to form the Chessie System, and the Chessie and Family Lines systems merged to form the CSX Corporation. Similarly, the Northern Pacific, the Great Northern and the Chicago, Burlington & Quincy merged to form the Burlington Northern, which then absorbed the Frisco. The Norfolk & Western and the Southern Railway are now merged into the Norfolk Southern, and the Missouri Pacific has been merged into the Union Pacific. Finally, the Santa Fe and the Southern Pacific presently are seeking Interstate Commerce Commission approval to merge. The trend is clearly towards regionalization of the Nation's railroads, with a single dominant carrier in each region. Indeed, many industry experts maintain that this day already has arrived.

Another significant anticompetitive trend has been taking place in the area of joint rates and reciprocal switching arrangements. Without going into excessive detail, joint rates and reciprocal switching arrangements are means by which railroads have created competition. In regard to joint rates, suppose Railroad X offered single line service between points A and C, while Railroad Y only served point C but could connect with Railroad X at intermediate point B. Traditionally, Railroads X and Y would offer a joint rate between points A and C that would be competitive with Rail-

road X's single line rate and which would be lower than the combination of rates between points A and B and between points B and C:



In regard to reciprocal switching, suppose a particular shipper's plant (P) is located on the tracks of a particular railroad (X). Railroads X and Y would negotiate reciprocal switching arrangements that permitted Railroad Y access to the plant:



In turn, Railroad Y would permit similar access to Railroad X at another plant.

The result of joint rates and reciprocal switching arrangements was the creation of competitive alternatives for the shipper, so that the shipper would not be limited to the use of the services of a single carrier. Unfortunately, beginning around 1982 and continuing to the present day, many of the Nation's largest rail carriers have been unilaterally--and on a wholesale basis--cancelling joint rates[3/] and

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3/ E.g., ICC Docket No. 39176, The Chlorine Institute, Inc. v. The Atchison Topeka & Santa Fe Ry. Co., et al.

cancelling or restricting reciprocal switching arrangements[4/] in those situations where the cancelling carrier can perform the service single line. Many agricultural shippers have been affected severely by these practices, as there are many routes where now only a single carrier can perform the single line service. Each cancellation, in turn, further decreases the number of routes where competition previously had been available. This has resulted in the growth of railroad monopoly power.

Many shippers have awakened to discover that suddenly they must deal with a monopoly carrier rather than carriers facing competition for their traffic. As expected, these monopoly carriers are dictating the terms of the carrier/shipper relationship--the shipper has no transportation alternative but to accept the railroad's terms.

Systematic railroad consolidation and wholesale cancellation or restriction of joint rates and reciprocal switching--each harmful in its own way--have combined to threaten a stranglehold on competition in the railroad industry. Ironically, this change in railroad practices has occurred at a time when deregulation largely has ended public utility style regulation of the surface transportation industry. Shippers no longer

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4/ Id.

can expect to look to the Interstate Commerce Commission for protection against railroad monopoly activity.

Indeed, the present ICC has been instrumental in paving the way for much of the reduction in competition previously described. The Commission generally has favored the trend towards increased railroad consolidation. Moreover, the ICC thus far has refused to intercede against the cancellation of joint rates and reciprocal switching. In proceedings before the Commission's Suspension Board, the agency repeatedly has declined to investigate or suspend the relevant tariff publications and has denied a petition (supported by numerous shippers) to institute a general investigation of such practices.[5/] Moreover, a complaint filed with the ICC by the Chlorine Institute specifically challenging the cancellations and restrictions as unreasonable practices under the Interstate Commerce Act over a year ago has yet to be assigned for hearing.[6/] In view of the ICC's handling of these and similar proceedings the agricultural community and other shippers are less than optimistic about the ICC properly exercising its authority to curb the unlawful growth of railroad monopoly power.

5/ Ex Parte No. 445, Standards for Intramodal Competition, served July 7, 1983.

6/ ICC Docket No. 39176, The Chlorine Institute, Inc. v. The Atchison, Topeka & Santa Fe Ry. Co., et al..

For all these reasons, the shipping public must now look to other forums in order to limit the growth of rail monopoly power. The obvious means is the application of the antitrust laws to the railroad industry. Indeed, in the absence of regulation, relief under the antitrust laws is essential if competition is to remain a factor in rail transportation.

However, the antitrust laws as presently structured do not provide a feasible mechanism for addressing the problems created by railroad consolidation coupled with joint rate and reciprocal switching cancellations and related actions. For example, Section 1 of the Sherman Act (15 U.S.C. §1), which outlaws conspiracies and combinations in restraint of trade, requires a showing of concerted action. The unilateral cancellation of a reciprocal switching agreement or a joint rate--and no evidence of concerted cancellation activity has yet surfaced--cannot violate Section 1. Section 2 of the Sherman Act (15 U.S.C. §2), on the other hand, does condemn unilateral monopolization and attempted monopolization. However, it would be exceedingly difficult for a shipper-plaintiff to define the relevant market in such a way as to establish either existing monopoly power or a substantial likelihood that monopoly power will be achieved.

It is for this reason that TFI supports the passage of S.2417. The bill would clarify that it is unlawful for a rail carrier, with intent to monopolize, to deny a shipper

the use of tracks that afford sole access to the track of a competing railroad or the destination of the shipment. Moreover, the bill would conclusively presume the requisite intent if the railroad denied use of its track upon reasonable terms to a shipper and denied use of the track to an alternate carrier ready to transport the shipper's goods. Finally, the bill specifies what are reasonable terms for use of the defendant railroad's facilities. Taken as a whole, passage of S.2417 will reinstate for monopolized shippers the availability of the selection of carriers that existed prior to the recent onslaught of mergers and cancellations. In other words, S.2417 will restore much need competition to rail transportation.

Moreover, TFI notes that the bill is not a radical proposal. The concept of mandated access by competitors to the "essential facilities" of a monopolist has long been a part of antitrust law. Indeed, the concept dates from the landmark Terminal Railway case.[7/] In that case, brought under Section 1 of the Sherman Act, the Government alleged that several railroads had conspired to control all terminal facilities in, and thus access to and from, St. Louis. The Supreme Court, finding both that such a conspiracy existed

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7/ United States v. Terminal Railway Association, 224 U.S. 382 (1911).

and that the cost of building and maintaining bridges made the creation of alternate access routes impractical, ordered that all railroads seeking access to St. Louis be granted reasonable access to the terminal facilities. Relying on Terminal Railways, the federal courts have applied the essential facilities doctrine in pure monopolization cases as well.[8/]

Further, there is no technical impediment to granting access to one railroad over the tracks of another railroad. In fact, this is sometimes done in merger cases, where Interstate Commerce Commission approval of the consolidation is conditioned on the grant of trackage rights over the consolidated system to carriers outside the system, as a method of preserving competition. The grant of such trackage in merger and related cases has often been for hundreds of miles.[9/] In the Southern Pacific-Santa Fe merger,[10/] numerous

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8/ E.g., MCI Communications Corp. v. AT&T Co., 708 F.2d 1081, 1132 (7th Cir.), cert. denied, -U.S.- (1983); Hecht v. Pro-Football, Inc., 570 F.2d 982, 992-93 (D.C. Cir. 1977), cert. denied, 436 U.S. 956 (1978); Mishawaka v. American Electric Power Co., 465 F. Supp. 1320, 1336 (N.D. Ind. 1979), aff'd. in relevant part 616 F.2d 976 (7th Cir. 1980), cert. denied 449 U.S. 1096 (1981).

9/ E.g., Union Pacific Corporation--Control--Missouri Pacific Railroad Company, 366 I.C.C. 459, 572-78 (1982), appeal pending (619 miles); Chicago & N.W. Transp. Co.--Construction--Wyoming and Nebraska, 303 I.C.C. 906 (1981), aff'd. No. 82-2341 (D.C. Cir. 1982) (76 miles); F.D. 29186, Chicago, Milwaukee, St. Paul & Pacific R. Co. (Richard B. Olgilvie, Trustee)--Trackage Rights--Illinois and Indiana,served January 24, 1980 (176 miles).

10/ ICC Finance Docket 30400, Southern Pacific Santa Fe Corporation--Control--Southern Pacific Transportation Company (still pending).

competing railroads are seeking significant trackage rights over the merged system, including the Union Pacific System, the Denver & Rio Grande Western R. Co., and the Missouri-Kansas-Texas R. Co.

While the ICC on occasion thus has been willing to impose trackage rights conditions, such provisions have not been automatic and generally have not been designed to eliminate railroad monopoly power. These ICC mandated trackage rights thus have been ineffective in preserving competition. Moreover, the grant of limited trackage rights as part of a merger proceeding will not protect the public against future anticompetitive activity.

In summary, the passage of S.2417 will mandate access to closed transportation facilities, thereby restoring intrarail competition and prohibiting railroad monopoly power.

Senator DECONCINI. Thank you, Ms. L'Italien. We appreciate your position and the material that you gave us will be very helpful.

Mr. Wallace?

STATEMENT OF DARRELL R. WALLACE

Mr. WALLACE. Mr. Chairman, my name is Darrell Wallace and I am director of Transportation for Union Equity Cooperative Exchange, a farmer-owned cooperative headquartered in Enid, OK. I am pleased to appear here today in my capacity as vice chairman of the National Council of Farmer Cooperatives' transportation committee.

The national council supports the goals embodied in S. 2417, and commends Senators DeConcini and Baucus for its introduction. Rail deregulation cannot function without adequate competition, and Government has the responsibility to restore competitive pricing and service where the marketplace cannot due to monopoly conditions.

S. 2417 represents an intriguing approach and the national council welcomes the opportunity to work with this committee. The national council continues to support the Staggers Rail Act's fundamental premise that the Nation's railroads must be economically healthy and should operate within the discipline of a competitive marketplace without excessive Government regulation.

In areas where intermodal and intramodal competition exists, the Staggers Act is functioning reasonably well for farmer cooperatives. However, agricultural shippers are growing increasingly

alarmed over the failure of the ICC to administer captive shipper provisions of the Staggers Act as intended by Congress.

The national council believes that the ICC has side-stepped its congressional mandate that it preserve and foster effective competition. Our particular areas of concern include revenue adequacy, market dominance, reciprocal switching, joint rates and routes, and contract disclosure.

Railroad ratesetting is a serious farm income issue. Farmers are price-takers and not price-makers, and increased transportation costs are absorbed by the farmer. In the case of grain marketing, as rail rates and reciprocal switching charges increase, the farmer simply receives a lower grain price.

In addition, any transportation cost increases absorbed by farmer cooperatives also result in reduced patronage dividends for farmers. The National Council is particularly concerned about the ICC technique used to determine rail revenue adequacy.

There is not a single class I railroad that is rated revenue-adequate by the Commission. Yet, several railroads have made major investments outside the industry. Railroad pricing practices can also determine the market area available to shippers by manipulating joint rates and routes and reciprocal shipping charges and selectively awarding contracts.

For example, a farmer cooperative has seen its reciprocal switch charge for jumbo covered hoppers jump to $204 per car, a 1,033-percent increase over 4 years. This cost represents about 6 cents per bushel. Yet, cooperative profit margins are slim and sometimes are as small as a fraction of a cent a bushel.

As a result, the cooperative is unable to buy grain from its own local member elevators on other lines and is captive to one rail carrier. The National Council believes this constitutes a restraint of trade and a reduction of competition among railroads.

The potential for such abuses on a widespread basis has been temporarily hindered due to the present hopper car surplus and weak demand for U.S. farm products. However, today's examples of rail abuses are signals of far greater problems that will become painfully evident as rail car supplies shrink relative to demand.

The problem that we as captive agricultural shippers face today is similar to that of a charging bull. You know darned well what will happen if the bull hits you. Do you wait for him to strike before taking any corrective action, or do you get out of the way, effectively dealing with the problem?

In conclusion, Mr. Chairman, the fate of farmers and other captive shippers lies in the hands of Congress. Failure on the part of Congress to take timely corrective action will mean even greater shock waves through the agricultural marketing chain, shrinking farm income, and reduced competition among railroads in the near future.

The National Council regards S. 2417 as a step in the right direction and stands ready to work with this Congress in achieving passage of needed Staggers reform legislation. Thank you.

[The prepared statement follows:]

Statement of
The National Council of Farmer Cooperatives
Before the
Senate Committee on the Judiciary
Presented by
Darrell R. Wallace
Vice Chairman, NCFC Transportation Committee
On S. 2417
The Consumers Railroad Transportation Antimonopoly Act

Mr. Chairman, my name is Darrell Wallace, and I am director of transportation for Union Equity Cooperative Exchange, a farmer-owned cooperative headquartered in Enid, Oklahoma. I am pleased to appear before this Committee today in my capacity as Vice Chairman of the National Council of Farmer Cooperatives' Transportation Committee. This Committee includes representatives of farmer cooperatives across the nation who are vitally dependent upon rail, trucks, inland waterways and ports for the movement of agricultural inputs and commodities.

Union Equity represents 697 country cooperative elevators, all owned by farmers, in Arkansas, Colorado, Kansas, Missouri, Nebraska, New Mexico, Oklahoma and Texas. Via our Houston grain terminal, Union Equity Cooperative exports about 20% of total U.S. wheat--more than any other cooperative grain shipper in the country. In total, we handle about 89,000 hopper carloads of wheat and milo each year between interior elevator origins and interior/export destinations.

INTEREST OF THE NATIONAL COUNCIL

The National Council of Farmer Cooperatives is an association of cooperative businesses which are owned and controlled by farmers. Our membership includes 107 major marketing and farm supply cooperatives, the 37 banks of the cooperative Farm Credit System, and 32 state councils of farmer cooperatives. The National Council represents about 90 percent of the 6,100 local farmer cooperatives in the nation, with a combined membership of nearly two million farmers.

Cooperatives are in the business of supplying inputs, and transporting and marketing commodities for their farmer-owners. Not only does this system carry with it a unique accountability, but it also directly ties the costs of doing business across the food system

to the farmer. Cooperatives by definition are non-profit institutions which rebate savings to farmer-owners in the form of patronage refunds. Increased cost of doing business translates into lower savings for farmers.

Farmer cooperatives play a critical role in transporting farm inputs and production. Cooperatives move over 70% of all U.S. milk and milk products, almost 50% of total U.S. grain and soybean production and 25% of the nation's fruits and vegetables. They transport 36% of U.S. fertilizer and lime, and supply 45% of on-farm fuel requirements.

SUMMARY OF STATEMENT

We commend this Committee for holding today's hearing on S. 2417. This bill highlights the need for a legislative solution to captive shipper concern over growing evidence of lack of rail competition and inadequate ICC implementation of the Staggers Rail Act.

This statement covers the following major points:

- NCFC support for the general intent of S. 2417.
- NCFC support for the Staggers Act and a strong, healthy U.S. rail industry.
- ICC failure to properly administer the captive shipper provisions of the Staggers Act.
- Reasons for farmer cooperative concern over present implementation of Staggers Act.
- The need for legislative change to promote railroad competition and reduce the potential for rail abuse of captive shippers.

NCFC SUPPORT FOR S. 2417

NCFC supports the goals embodied in S. 2417 and commends Senators DeConcini and Baucus for introducing the bill. Farmer cooperatives support legislative change to promote rail competition and to reduce the anti-competitive opportunities for rail carriers that exist now at the expense of captive shippers. Railroad deregulation cannot function without adequate competition...and government has the responsibility to restore competitive pricing and service where the marketplace can not, due to monopoly conditions. S. 2417 represents an intriguing approach, and NCFC welcomes the opportunity to work with your Committee on this important issue.

FARMER COOPERATIVE SUPPORT FOR STAGGERS ACT

The National Council supported passage of the Staggers Rail Act in 1981. We continue to support the law's fundamental premise that the nation's railroads must be economically healthy and should operate within the discipline of the competitive marketplace without excessive government regulation. A strong, viable U.S. railroad industry is essential for railroads to continue to serve as a vital marketing link for American agriculture. Without adequate rail service, neither farmers nor shippers could satisfy demand for U.S. food and fiber because many areas do not have competitive transportation alternatives. Last year, Class I railroads alone hauled 48% (4.7 billion bushels) of America's 9.7 billion bushel grain crop.

In areas where intermodal or intramodal competition exists, the Staggers Act is functioning reasonably well for farmer cooperatives. Our concern lies with the "captive" shipper who must market grain and more farm inputs without the benefit of healthy competition. In its opening statement in the Staggers Act, Congress declared that "...it is the policy of the U.S. government to maintain reasonable rates where there is an absence of effective competition and where rail rates provide revenues which exceed the amount necessary to maintain the rail system and attract capital." Specific provisions were included in the final law to implement this policy.

ICC IMPLEMENTATION OF STAGGERS ACT

However, agricultural shippers are growing increasingly alarmed over the failure of the Interstate Commerce Commission to properly administer these captive shipper provisions of the Staggers Act as intended by Congress. NCFC believes the Commission has sidestepped its Congressional mandate that it preserve and foster effective competition in the railroad industry. Our specific concerns stem from the ICC's actions (or lack of action) on revenue adequacy, market dominance, reciprocal switching, joint rates and routes, and contract disclosure. Agricultural cooperatives have spent large sums on legal fees in cases before the ICC, with no positive results. Indeed, the NCFC believes that the ICC is so unresponsive to shipper concerns our members no longer waste scarce farmers' dollars on ICC proceedings.

REASONS FOR FARMER COOPERATIVE CONCERN OVER STAGGERS ACT IMPLEMENTATION

Farmer cooperative concern over ICC misinterpretation of Congressional intent of the Staggers Act focuses on rail cost and serivce. Railroad pricing is a serious farm income issue. Farmers are "price takers," not "price makers," and increased transportation costs cannot be passed on automatically to the consumer. The grain marketing chain offers the farmer a per bushel price that excludes transportation cost, since the price of grain is determined largely by the price destination (Gulf or Pacific Coast). The producer receives less per bushel the farther he is located from either of these locations due to higher transportation cost for his grain. Thus, as rail rates and reciprocal switching charges increase, the farmer simply receives a lower grain price. The price of farm inputs, such as fertilizer and seed, is also higher, increasing farm production costs. In addition, any transportation cost increases absorbed by farmer cooperatives result in reduced patronage dividends returned to farmer-members. Therefore, the farmer is placed in triple jeopardy by rail price increases.

Contrary to the intent of the Staggers Act, captive agricultural shippers have also been unable to prove that a rail rate is unreasonably high due to ICC techniques used to determine rail revenue adequacy. The Staggers Act allows a rail carrier to establish any rate for transportation unless it has market dominance, in which case the rate must be reasonable. Congress also directed the ICC to recognize the law's intent that carriers earn adequate revenues in determining rate reasonableness. In determining whether a railroad is revenue adequate, or profitable, the ICC decided to consider only one economic factor, the railroad's rate of return on investment versus the current cost of capital. However, there is not a single Class I railroad that is rated revenue adequate by the Commission even though several railroads have made substantial investments outside the industry. For this reason, the Commission needs to redefine its use of rate of return to more accurately reflect actual profitability.

Even though the ICC continues to find all major railroad technically unprofitable, the railroads themselves do not. The American

Association of Railroads recently reported that rail income jumped dramatically for the first quarter of 1984 compared to the same period last year. Ordinary rail income was up 250%, while net income increased 114%. A strong and profitable railroad system does not mean extracting monopoly rent from American farmers to create excess profits or fund outside investments.

Railroad pricing practices can also determine the market area available to shippers. Today, railroads effectively have the ability to dictate joint rates and routes, reciprocal switching charges, and which shipper can get a contract on what terms. Faced with the inability of captive shippers to negotiate in return, rail carriers are empowered to determine which farmer cooperatives are able to market their members' grain and which cannot.

The following example illustrates this point. A farmer cooperative faced a reciprocal switching charge of $18 per jumbo hopper car in 1981. The full switching charge was absorbed by the receiving rail carrier and not charged to the shipper. Today, the switching charge has jumped to $204 per car, a 1,033% increase over four years. Moreover, the receiving carrier will not absorb more than the original $18 per car. The cooperative is faced with the dilemma of either paying the remaining $186 per car or not buying any switched grain from its members. The cost of this additional switching charge is about 6¢ per bushel; yet cooperative profit margins are slim, only about 2¢-3¢ per bushel ($66-$99 per car). As a result, the cooperative is unable to buy switched grain from its local elevator-members and is captive to one rail carrier due to excessive switching charges. NCFC believes this constitutes a restraint of trade and a reduction of competition among railroads.

The impact of the Staggers Act on captive agricultural shippers has been softened since passage of the law due to a hopper car surplus and weak demand for U.S. farm products. To cover fixed costs of operation, some rail carriers have been willing to offer shippers acceptable rates and contracts. However, today's examples of rail abuse spell even more problems that will become painfully evident, especially to captive shippers, as rail car supply shrinks relative to demand. That process is already starting this fall due to strong Soviet wheat and feed grain purchases needed to compensate for a short USSR grain crop.

NEED FOR LEGISLATIVE CHANGE

The situation of the major railroads and captive agricultural shippers is similar to a bull charging...do you wait for him to hit and see what it feels like or do you get out of the way, solving the problem? We urge Congress to take action to promote more rail competition and effective captive shipper treatment since based on past performance, the ICC does not. Failure to do so now will mean even greater shock waves through the agricultural marketing chain, shrinking farm income and reduced competition among railroads in the near future.

In conclusion, Mr. Chairman, the fate of farmers and other captive shippers lies in the hands of Congress. The National Council regards S. 2417 as a step in the right direction, and stands ready to work with you to encourage passage of needed Staggers reform legislation. Thank you for this opportunity to appear before you today. I will be pleased to answer any questions you may have.

Senator DECONCINI. Thank you.
Mr. Harding.

STATEMENT OF WILLIAM C. HARDING

Mr. HARDING. My name is William C. Harding. I am vice president of transportation for the Louis Dreyfus Corp. of Stamford, CT. As chairman of the transportation committee of the National Grain & Feed Association, I am here today to enter this statement on behalf of the association.

National Grain & Feed is a voluntary association of grain and feed firms ranging in size from the smallest country elevator to the largest grain and feed complex. Over the past decade, Congress has enacted legislation to help revitalize the Nation's railroad industry by reducing the regulatory presence of the Federal Government in the rail sector.

The nature of both inter and intramodal competition in the rail transportation marketplace has changed dramatically over the past few years, as have relationships between rail carriers and shippers. Some of the changes have been decidedly favorable, while others have created severe economic hardship.

But one fact has become increasingly clear; namely, that competitive alternatives for rail shippers are becoming increasingly vulnerable to the actions and decisions of the rail industry in our present deregulated environment, and the opportunity for redress before the Interstate Commerce Commission continues to diminish.

The grain industry has been particularly hard hit by the closure of joint rates and routes and the cancellation or increased cost of switching charges because we ship the majority of our commodities

by rail. In most instances, grain elevator facilities find themselves dependent upon a single rail carrier for their transportation service.

In March of 1983, the National published a survey of grain transportation which illustrates the severity of the problem for grain shippers. The results of that survey indicate that of all the country elevators in the sample that are served by rail, 94.3 percent are served by a single railroad.

Terminal elevators also are dependent to a significant degree on a single railroad to provide their transportation needs. In fact, 63.5 percent of these facilities that are served by rail have direct access to only one rail carrier, but nearly half of these terminal elevators have the potential to take advantage of traffic interchange within their city's switching limits if switching agreements are maintained by the carriers.

This demonstrates the importance of access to open switching to all segments of the grain industry. A number of factors have contributed to the problems faced by grain shippers in their relationship with rail carriers, but the main contributing factor is a lack of enforcement of current law on the part of the Interstate Commerce Commission.

To better demonstrate these problems, I would like to share the following examples of the railroads' anticompetitive behavior with you, and describe the economic hardships being experienced by our members. More examples exist, but these few adequately illustrate the problem.

In one midwestern market, an association member operates several elevators that are served either by Chessie, Conrail, or the Norfolk Southern. Disputes between these carriers on their joint rates and routes and switching have served to restrict both the grain purchasing activities and the markets to which these elevators may ultimately ship their grain.

Where their elevators are served by Conrail, the current situation is so bad that the facilities can only ship their grain to eastern markets, regardless of the potential to receive a better price for their grain elsewhere. The bottom line for this company has been revenue losses in excess of $1 million annually because of the current uncooperative actions of regional carriers.

A Chessie railroad official described this type of situation with the following words: "The loss of traffic is simply the application of Conrail's geographic muscle, with no justification in the way of cost savings."

An additional example comes from a large exporter of grains that operates nationwide. It has found that it can no longer originate grain on the Norfolk Southern for final delivery to its facility in Baltimore, MD, which is not open to reciprocal switching.

Prior to this year, between 40 and 50 percent of the grain shipments to this Baltimore elevator had originated on the Norfolk Southern. This year, the traffic likely will be handled solely by Chessie, meaning that the company is limited in its ability to originate grain for final delivery to Baltimore.

The negative impact in revenues cannot yet be calculated, but it is fair to say that it will be substantial. Switching charges refer to the cost of transferring cars of one railroad to the tracks of an-

other. This problem, along with joint rate cancellations, are blatant abuses by which carriers restrict shipper access to markets, with the intent to monopolize.

For example, one of our members has experienced switching charge increases from $10 to $298 per car. Certainly, those increases have nothing to do with the cost of providing the service.

Robert Claytor, chief executive officer of the Norfolk Southern, admits that current railroad actions are designed to monopolize traffic, and he indicates the universal nature of the situation in a statement to the press as follows: "Deregulation makes it imperative that you serve markets with your own line and not through connecting railroads. Other railroads are able to freeze you out of the market."

In general, railroads attempt to monopolize traffic or service by denying entry. They deny entry on their lines to existing and potential rail carriers through the methods I have just described, and they also attempt to deny entry of private hopper cars even though virtually all carriers encouraged grain shippers to acquire such cars when shortages existed throughout the 1970's.

National Grain and Feed in March of 1984 adopted a legislative plan with respect to a number of rail issues. Given that the ICC has failed to implement congressional intent, we firmly believe that a legislative solution is the appropriate course of action. We therefore support S. 2417, as well as any other legislation currently pending.

S. 2417 would increase competition among rail carriers, thereby ensuring that rail shippers can experience reasonable rates and services through the working of competitive market forces. It also assures captive shippers adequate access to markets.

The National supports legislative action that will prevent railroads from engaging in anticompetitive practices. Thank you.

[The prepared statement follows:]

NATIONAL GRAIN & FEED ASSOCIATION

STATEMENT OF

THE NATIONAL GRAIN AND FEED ASSOCIATION

BEFORE THE

COMMITTEE ON JUDICIARY

UNITED STATES SENATE

ON S. 2417

SEPTEMBER 18, 1984

My name is William C. Harding. I am Vice President of Transportation for the Louis Dreyfus Corporation of Stamford, Connecticut. As chairman of the Transportation Committee of the National Grain and Feed Association, I am here today to enter this statement on behalf of the Association.

The National Grain and Feed Association (NGFA) is a voluntary association of grain and feed firms ranging in size from the smallest country elevator to the largest grain and feed complex. Included in its membership are country and terminal elevators, merchandisers, processors and exporters covering the wide spectrum of the grain and feed industry. The Association's membership is comprised of 1,300 companies and 44 affiliated state and regional grain and feed associations that include more than 10,000 grain and feed companies nationwide.

Over the past decade, Congress has enacted legislation to help revitalize the nation's railroad industry by reducing the regulatory presence of the federal government in the rail industry. Unfortunately, certain anti-competitive actions by the railroads in recent years have demonstrated their desire to restrain competition in markets where they enjoy sufficient economic leverage. These actions include:

-- rate discriminations between similarly situated shippers through the use of secret contracts;

-- unreasonable pricing practices in markets where a single carrier is dominant; and,

-- economically unjustifiable abandonments of rail branch lines.

But potentially the most onerous and anticompetitive actions by the nation's rail carriers are those relating to the closing of joint rates and routes; the discouragement of traffic interchange through the cancellation of

switching agreements or the setting of switching charges at exhorbitant levels; and, actions taken by rail carriers to discourage the use of, and fair compensation, for shipper rail cars. Such deteriorations of intra-modal competition are intolerable in a free market economy. It is for these reasons that the National Grain and Feed Association supports the amendments to the Sherman Act contained in S. 2417 as an appropriate measure to restore competitive rail transportation service in this country to the benefit of rail carriers and shippers alike.

The nature of both inter- and intra-modal competition in the rail transportation marketplace has changed dramatically over the past few years, as have relationships between rail carriers and shippers. Some of the changes have been decidedly favorable, while others have created severe economic hardship. But one fact has become increasingly clear. Namely, that competitive alternatives for rail shippers are becoming increasingly vulnerable to the actions and decisions of the rail industry in our present deregulated environment, and the opportunity for redress before the Interstate Commerce Commission continues to diminish.

The grain industry has been particularly hard-hit by the closure of joint rates and routes and the cancellation or increased cost of switching agreements. Numerous instances of inter-carrier disputes exist where the victim is the shipper who loses access to potentially profitable markets. The reason that this places such an economic burden on the grain industry is that we ship the majority of our commodities by rail and in most instances, grain elevator facilities find themselves dependent upon a single rail carrier for their transportation service.

In March 1983, the National Grain and Feed Association published a survey of grain transportation, which illustrates the severity of the problem for grain shippers. The results of that survey indicate that not only is the grain industry heavily dependent on the rail mode, but to a great degree, grain shippers are dependent upon a single carrier within the rail mode. In fact, of all country elevators in the sample that are served by rail, 94.3 percent are served by a single railroad. But, the problem does not end with country elevators. Our survey shows that terminal elevators also are dependent to a significant degree on a single railroad for their transportation needs. In fact, 63.5 percent of these facilities that are served by rail have direct access to only one rail carrier, but nearly half of these terminal elevators, that are served by

one railroad, have the potential to take advantage of traffic interchange within their city's switching limits if switching agreements are maintained by the railroads. This demonstrates the importance of access to open switching to this segment of the grain industry.

NGFA's survey shows that all types and sizes of grain shippers, regardless of geographical location, can be affected by the anticompetitive actions of the railroad industry. But, even if the scope of the problem were not as wide, those shippers that are dependent on a single railroad would be no less harmed. Given this situation, one easily can see that the maintenance of competition among railroads is the only way that grain shippers can retain access to competitive markets and access to competitive rail service at a reasonable cost.

Critics might argue that grain shippers can gain access to markets and competitive transportation service by shipping via truck or barge. However, as a practical matter, this frequently is not possible. First, the majority of grain shippers are not located contiguous to a navigable waterway. Second, studies have shown that trucking grain to a barge loading point is economically feasible only when the elevator is just a short distance from the waterway. Third, truck shipments of grain generally are viable only for relatively short distance movements. Motor carriage is the most costly method by which grain moves, and it would take nearly 300 large trucks to do the job of a 75-car unit train in shipping grain for export or domestic use. This option simply does not make economic sense.

A number of factors have contributed to the problems faced by grain shippers in their relationships with rail carriers, but the main contributing factor is the lack of enforcement of current law on the part of the ICC and the increasing monopoly power on the part of the railroads resulting from the level of concentration in the industry that has been caused by a series of railroad mergers that have reduced the number of competitors and the level of competition in the industry. This problem is exacerbated in cases where rail mergers have been parallel rather than end-to-end. The spirit of comraderie and cooperation that once existed among railroads is gone, and it has been replaced by a situation that can only be described as destrucitve. This situation produces no clear winners and serves to ensure that rail shippers are the clear losers in terms of lost markets and lost revenues. In reference to this issue, ICC Commissioner Heather Gradison has stated that, ". . . .joint rates and routes, interchange agreements, reciprocal switching and car service and car hire rules

are the sinews and ligaments that tie the parts into a whole. These links create many situations in which railroads must at the same time -- cooperate and compete." Unfortunately, cooperation is currently missing from the equation, and rail carriers are demonstrating that they also would like to eliminate competition through the exercise of any market power they are able to muster.

To better demonstrate these problems, I would like to share the following examples of the railroads' anticompetitive behavior with you and describe the economic hardships being experienced by our members. More examples exist, but these few adequately illustrate the problem.

In one Midwestern market, an Association member operates several elevators that are served by either Chessie, Conrail or the Norfolk Southern. Disputes between these carriers in the area of joint rates and routes and switching have served to restrict both their grain purchasing activities and the markets to which they may ultimately ship their grain. For their elevators served by Conrail, the current situation is so bad that those facilities can only ship their grain to Eastern markets, regardless of the potential to receive a better price for the grain elsewhere. This particular company chose to build its facilities in locations where they could receive the benefits of competitive rail service. But recent carrier actions have thwarted the realization of the expected benefits. The bottom line for this company has been revenue losses in excess of $1 million annually because of the current uncooperative actions of their regional carriers. A Chessie Railroad official described this type of situation with the following words: "The loss of traffic is simply the application of Conrail's geographic muscle with no justification in the way of cost savings."

An additional example comes from a large exporter of grains that operates nationwide. It has found that it can no longer originate grain on the Norfolk Southern for final delivery to its facility in Baltimore, which is not open to reciprocal switching. Prior to this year, between 40 and 50 percent of the grain shipments to this Baltimore elevator had originated on the Norfolk Southern. This year, the traffic likely will be handled solely by Chessie meaning that the company is limited in its ability to originate grain for final delivery to Baltimore. The negative impact on revenues cannot yet be calculated, but it is fair to say that it will be substantial.

Other examples are readily available concerning the issue of switching. In circumstances where shippers once were able to gain access to markets through the interchange of traffic, increased switching charges have removed these

opportunities. Switching charges refer to the cost of transferring the cars of one railroad to the tracks of another railroad. This problem, along with joint rate cancellations, are blatant abuses by which carriers restrict shipper access to markets with the intent to monopolize. For example, one of our members has experienced switching charge increases from $10 to $298 per car. Certainly these increases have nothing to do with the cost of providing the service. When the shipper complained to the carrier involved, the railroad said they were simply responding in-kind to the actions of other carriers. The shipper further complained that the increases were implemented on grain traffic but not on other commodity shipments. The railroad's response was to increase the charges on the other traffic.

Another Association member that is engaged in grain export operations became involved in a dispute with the Burlington Northern Railroad (BN) concerning the switching of empty Santa Fe Railroad cars at a grain elevator in Enid, Oklahoma. BN had maintained reciprocal switching arrangements with Santa Fe at this location for some 40 years or more whenever the shipper required empties for outbound line-haul movement on the Santa Fe. Based on established carrier practice, the shipper, in December 1982, negotiated a contract with Santa Fe for a rate reduction on wheat shipments from Enid. This favorable rate was only available if Santa Fe cars were used and the rate increased substantially if cars of other railroad ownership were used. In January 1983, BN notified the shipper that it was terminating its past practice of open switching for Santa Fe cars at the shipper's Enid facility. The move obviously hampered the operation of a contract that was negotiated in good faith. The shipper challenged BN in U.S. district court and before the ICC and the district court rendered a favorable decision in late May of this year, which is now under appeal. The example is demonstrative of disruptive, unilateral carrier actions on which considerable time and money were expended in the disposition of the matter. Few grain companies are able to devote the needed resources to such a course of action.

These examples not only demonstrate the severity of the problems faced by shippers, but they also show that anticompetitive actions with the intent to monopolize are actively and extensively practiced by the railroad industry. Numerous examples exist whereby a line-haul between two cities theoretically could be performed by a number of different carriers. But in reality it does not happen because the terminal point at the city of destination may be closed

to switching. This simply means that the cars of the line-haul carrier cannot be switched to the track of the railroad that directly serves a destination elevator. The shipper then has no choice but to originate grain from locations served by a carrier that also can serve the desired destination. The shipper and/or receiver of grain therefore is subject to the monopoly actions of the railroads and his marketing opportunities become unreasonably constrained.

Robert Claytor, Chief Executive Officer of Norfolk Southern, admits that current railroad actions are designed to monopolize traffic. And, he indicates the universal nature of the situation in a statement to the press as follows: "Deregulation makes it imperative that you serve markets with your own line, and not through connecting railroads. . . .other railroads are able to freeze you out of the market." The problem from our perspective is that railroad actions such as these also freeze grain and other commodity shippers out of markets.

In general, railroads attempt to monopolize traffic, or service, by denying entry. They deny entry on their lines to existing and potential rail carriers through the methods I have just described. And, they also attempt to deny entry to private hopper cars in an effort to monopolize carriage in their own equipment, even though virtually all carriers encouraged grain shippers to acquire such cars when shortages existed throughout the 1970s.

The present covered hopper car situation, which can be described as one of excess supply, has prompted railroads to discourage the use of private equipment through discriminatory tariffs or through paying unfair levels of compensation to private car operators. But spot shortages do exist and will continue to exist in grain-carrying capacity. If railroads effectively discourage the use of private grain cars and prompt shippers to retire equipment or not renew private car leases, then carriers will be in a position to extract monopoly profits from shippers in instances when car shortages exist. This is both unfair and contrary to the objective of allowing market forces to operate. Once again, rail carriers are attempting to inhibit competition for the purpose of monopolizing rail services.

Private car compensation is negotiated between carriers and shippers, and these negotiations currently are subject to regulations included in the Interstate Commmerce Act. However, it has become apparent to those who are negotiating the terms of private car use that the railroads ultimately desire to have car compensation totally deregulated. If they are successful in this regard, the only recourse available to shippers will be antitrust laws such as

the proposal being discussed today. Again, the potential losses that could be borne by private car operators due to railroad restrictions amount to millions of dollars.

The National Grain and Feed Association, in March 1984, adopted a legislative plan with respect to a number of rail issues. It is our belief that recent railroad actions that have been implicitly sanctioned by the ICC by its failure to act have been in contravention of the intent of Congress. Given that the ICC has failed to carry out properly the duties charged by Congress, we firmly believe that a legislative solution is the appropriate course of action. We, therefore, support this measure as well as several others currently pending. Most notably, we support H.R. 5731, "The Railroad Deregulation Improvement Act of 1984," introduced by Congressman Ron Marlenee of Montana and cosponsored by Congressman Pat Roberts of Kansas.

H.R. 5731 embodies the goals and policies of our association with respect to competition in the rail industry, and it would go a long way towards ensuring that shippers and carriers alike will realize the benefits of competition.

Regarding joint rates and through routes, the adopted policy of the National Grain and Feed Association calls for the provision and maintenance of at least one through route between such origins and destinations where more than one carrier is able to participate in the movement. Our policy further asserts that if two or more rail carriers cannot agree on the terms of a joint movement, the ICC shall, upon complaint, prescribe such conditions as are necessary to make such service available to shippers.

With respect to switching, our policy states that switching at a reasonable cost should be the absolute right of every shipper in order to protect competition in all markets where more than one carrier is physically present.

Finally, we support the encouragement of new rail entry through the acquisition of operating rights and, on the issue of equipment supply, we suport a national system of compensation and use that treats fairly and equally both railroad and shipper cars while promoting a competitive, demand-sensitive equipment market.

S. 2417, embodies our position through the amendment of the Sherman Act and makes it illegal for railroads to deny access to their facilities with the intent to monopolize. S. 2417 would increase competition among rail carriers, thereby, ensuring that rail shippers can experience reasonable rates and services through the working of competitive market forces. It also gives shippers

more adequate access to markets and allows them to choose among a wider array of transportation alernatives. The National Grain and Feed Association, supports legislative action, such as S. 2417, that will prevent railroads from engaging in anticompetitive practices.

I will be happy to answer any questions of the committee.

SUPPLEMENTARY COMMENTS TO
STATEMENT OF
THE NATIONAL GRAIN AND FEED ASSOCIATION
BEFORE THE
COMMITTEE ON JUDICIARY
UNITED STATES SENATE
ON S. 2417

The National Grain and Feed Association, a voluntary association of grain and feed firms, offers the following comments to supplement the hearing record on S. 2417.

S. 2417 is an appropriate measure to restore competition to rail transportation and to ensure that rail shippers with limited transportation options enjoy the benefits of that competition. All shippers of low value bulk commodities are heavily dependent on the rail mode, especially in circumstances where geographic, seasonal or capacity limitations render barge transportation an ineffective option. Grain is no exception and statistical survey results also demonstrate that the vast majority of grain shippers with access to rail service are served by only one rail carrier. This fact gives rise to a problem currently being faced by numerous rail shippers. Namely, that rail carrier actions in various markets have served to restrict traffic, originating on the lines of a certain carrier, to destinations that may or may not be served by the origin carrier. This hinders the ability of grain shippers, and others, to effectively market their commodities in markets that present the most favorable opportunities.

Railroads accomplish transportation restrictions through the closing of joint rates and routes, through cancelling or increasing the cost of switching agreements, and by restricting the use of shipper hopper cars and, in some cases, even competing cars of another railroad.

This type of activity is very curious considering that the railroad industry worked so diligently and cohesively in persuading Congress to allow market forces and competition to replace the presence of government in regulating the rail transportation marketplace. The presence of government has been substantially reduced, but the railroads are doing a good job of limiting competition and the operation of market forces. The full statement of the National Grain and Feed Association to the Judiciary Committee includes a number of examples that demonstrate this phenomenon.

Opponents of this legislation continually attempt to confuse the issue by asserting that such corrective action would be a return to burdensome government regulation of the railroad industry. But, this is not the case. The issue here is competition, and recent carrier actions have demonstrated their unwillingness to compete. In addition, the problem is not necessarily one of unreasonable rates being charged. Rather, the problem is one of rail shippers being unable to effectively market their commodities unimpeded by artificial, anti-competitive barriers being erected by the railroads. Closure of joint rates and routes, unjustified switching charge increases and private car use restrictions are all examples of individual railroad actions that serve to isolate them from the competitive pressures of the marketplace.

This bill would not place a regulatory burden on railroads. It would, however, put an end to self-serving carrier practices that cause distortions in the marketplace. If railroads truly believe that competition is the most efficient regulator, then they have nothing to fear from S. 2417. The bill simply restores competition in areas where rail-dependent shippers have been subject to the anti-competitive actions of the railroads. To this end, the National Grain and Feed Association supports the amendments to the Sherman Act contained in S. 2417.

Senator DECONCINI. Thank you very much, Mr. Harding. All of your testimony is extremely helpful. I do have a few questions. I notice the ranking member of the committee is here. Does he have a statement or care to make any comments?

Senator BIDEN. No.

Senator DECONCINI. Thank you.

Ms. L'Italien, may I ask you, has your organization made any attempts to have the ICC resolve the difficulties you have laid out in your testimony?

Ms. L'ITALIEN. Not the Fertilizer Institute, as I speak in their behalf today. However, the company that I work for has made several attempts to have the ICC resolve rate dispute cases since the passage of the Staggers Act.

Senator DECONCINI. And what have been the results of those attempts?

Ms. L'ITALIEN. For the most part, they have not yet been resolved. I would characterize them as one constant delay after another, with rules which change midstream where the Interstate Commerce Commission has required of shippers or of protestants to bring in additional evidence.

For example, the stand-alone costs or coal rate guidelines have recently come out that have yet to be finalized.

Senator DECONCINI. Mr. Wallace, your organization and members—with the advent of the current trend of the railway mergers across the Nation that we have witnessed, has there been an effect with your organization as to the price of your goods and the transportation equation in that price other than just the case we have before us? Do you have several examples of where that has occurred?

Mr. WALLACE. Well, I think we have seen joint rates and routes not necessarily closed, but they have priced us out of the market.

Senator DECONCINI. Now, when you say priced you out of the market, does that mean that you stopped shipping or that you just cannot sell as much?

Mr. WALLACE. On grain, you know, a sale could be won or lost on a matter of an eighth of a cent a bushel. So if you have got any transportation cost that is higher in one direction than it is in another, then effectively you cannot compete in that market.

And with these mergers, we have seen cases where we have had four or five alternate routes to different destinations and now we are locked in to only one carrier.

Senator DECONCINI. And the price has gone up as a result.

Mr. WALLACE. You know, in essence, the joint rate is still there, and the joint route, but the price for that joint route is much higher than if you went single route to another destination. So, effectively, they have cut you out of markets.

Senator DECONCINI. Is it just the obvious reason that the agricultural shippers of farm-related products so heavily depend on rail transportation because there is nothing else?

Mr. WALLACE. We do have some other alternatives, but I can only really speak as far as my particular company. We handle about 88,000, 89,000 carloads of grain a year, and if you equate that to trucks, you are talking 250,000 trucks on the highways.

No. 1, you cannot find truck drivers; you could not find that many trailers; you could not find that many tractors. You would beat up the highways. We would have a problem with diesel.

The most effective way of moving bulk grain is via the railroads. Therefore, we are captive shippers to the railroads.

Senator DECONCINI. Do you move bulk grain by truck? Is that accomplished to any magnitude?

Mr. WALLACE. There is quite a bit of bulk grain moved by truck; yes.

Senator DECONCINI. Is that a growing way of transporting it?

Mr. WALLACE. We have seen it, I guess, grow somewhat with the contracts. The railroads like to foster flat, nontransit contracts which foster truck movement into a terminal with unit trains beyond.

As far as trucking to the gulf for export, I do not believe that has increased. Probably, if anything, that has diminished some. Our company has not trucked to the gulf in over 2 years.

Senator DECONCINI. Mr. Harding, I do not quite understand the joint rail rate cancellations. It is supposed to improve railroad efficiency by promoting single-line service over joint lines; is that correct? Is that your understanding?

Mr. HARDING. The intent, I think, was to throw out a lot of the superficial routes and rates that were in existence.

Senator DECONCINI. Why, in your opinion, has that not worked?

Mr. HARDING. I think the key issue is competition in entry. You just do not have competing carriers that can come in and keep them honest, and so if they have the power to restrict your markets that you can serve by canceling joint rates and routes or by increasing switching charges, they are going to do it.

It is just human nature to capitalize on what advantage you have, and in their case the advantages can be quite extensive.

I would like to comment on the barge and truck competition. Barge competition has capacity limits and geographic limits. Truck competition, as Darrell said, is primarily in the short distances and is not effective in hauling grain for long distances.

Senator DECONCINI. Senator Biden.

Senator BIDEN. Thank you, Mr. Chairman.

Senator Baucus had to go to the floor and he asked if I would ask a question of Mr. Wallace. Since your cooperative, Union Equity, is the largest Hard Red Winter wheat exporter in the country and you have vast quantities of grain, why can you not use your market power to leverage and negotiate with the railroads for attractive prices and services?

Mr. WALLACE. I think the main reason is that we are not really sure—not being able to have contract disclosure, we are not really sure or convinced that we could actually negotiate a competitive contract.

The biggest problem is there are always bigger shippers. Since we deal 99 percent in exportation of bulk, raw grain, we would not have the market clout that other shippers would who deal in other commodities—fertilizer and farm supply goods.

There is always another guy out there that is a little bit bigger than you are who is going to be able to negotiate a better contract than what you can get. We did not really believe that the intent of

Staggers was to give preferential treatment to large shippers over the demise of the smaller shippers.

Senator BIDEN. If this question has been asked, I will read it in the record. What are some of the specific examples faced by Union Equity as a result of the implementation of the Staggers Act?

Mr. WALLACE. We have had a lot of problems as far as notices of rail rate increases. Rates are changed almost——

Senator BIDEN. Did they not change before?

Mr. WALLACE. Not as quickly as they do now, sir. Many times, rate increases are in effect for days or weeks before we even have notice that there is an increase.

Senator BIDEN. Is that new? That is not a new phenomenon in the history of rail rates, is it, or is it? You have got to educate me.

Mr. WALLACE. Generally, we had at least an advance notice that there was going to be a proposed change. Now, a lot of times they can come in with a change and publish it on short notice and get it in, in 1 day, get it effective on 1 day's notice, and you are never aware that it was coming.

Senator BIDEN. Is your argument that, in fact, these rate increases—these are my questions, not Senator Baucus'—are you, in fact, convinced that the rate increases you have, in fact, experienced are a consequence of you being a captive, or are reasonable?

The fact of the matter is there can be—and I am not making the case; I do not know. But what distinguishes between a rate increase that is justified because of other costs and other factors and a rate increase that—I have never known a shipper who likes a rate increase under any circumstances. I have never known a customer that likes a price increase under any circumstances.

So I would like you for the record to distinguish for me, at least, why you are convinced, if you are, that the rate increases you have recently experienced are a consequence of you now being in a different posture as a consequence of the Staggers Act than you were before the Staggers Act.

Mr. WALLACE. I think probably, to back just a little bit, No. 1, as far as in the bulk grain industry, we really have not seen rate increases; they have not been prevalent. In fact, just the opposite, we have had rate reductions. But we do not believe that any of these reductions were due to Staggers.

They were due to an overabundance of hopper cars; they were due to the Russian grain embargo. They were due to limited demand for agricultural exports. The railroads had idle cars out there; shippers were not moving anything. They came in and offered cheap contract rates just in order to get equipment moving.

So just the reverse has been true; we have had rate reductions and not necessarily increases. But we believe that when the situation turns around and cars become tight, we are probably going to be subject to some very high and substantial rate increases, with which we do not think we will have any effective means of defending ourselves.

Senator BIDEN. I guess my concern is whether this is a remedy looking for a wrong or a wrong exists and we are going to propose a remedy.

Mr. HARDING. I think the major issue here is competition, and there certainly is a lack of competition in the rail sector. What we

are here asking for is increased competition through the amendment to the Sherman Act to make sure that railroads do not use their market power to cancel joint rates and routes, to raise switching charges, to cancel reciprocal switching as a right, to force shippers not to use the private cars that they have leased 5, 10, 15, and 20 years.

Senator BIDEN. My question is, has any of that occurred yet?

Mr. HARDING. Yes; a lot of that has occurred, and we have given some examples here today.

Senator BIDEN. Give me some more.

Mr. HARDING. Some more examples?

Senator BIDEN. Yes.

Mr. HARDING. In which area, reciprocal——

Senator BIDEN. Yes; repeat them again for me.

Mr. HARDING. Well, my company has a facility in Baltimore, MD. The eastern carriers, the Norfolk Southern and the Chessie, this year are not apt to be able to agree on joint rates and routes into that facility. In the past, my facility has originated 40 to 50 percent of all its grain off the Norfolk Southern.

Both carriers have told me in the past that I am the low-cost facility to serve; that they make more money serving me than they do a competitor down in Norfolk. Yet, they are not able to cooperate and to publish joint rates and routes on a competitive basis into my facility, and that hurts me.

I do not think they should have that right to curtail the——

Senator BIDEN. It has hurt you already?

Mr. HARDING. It has hurt us already.

Senator BIDEN. In what specific way? How much grain have you not shipped?

Mr. HARDING. We are right now in the midst of gearing up for the grain harvest which will come off in October. We have been buying grain for our facility over the summer months. We have probably booked or bought a third to a half of all the grain we are going to handle through that facility in October, November, and December.

Because we do not have competitive rates in existence off the Norfolk Southern, we have been unable to buy 1 bushel of grain from facilities served by that carrier. That hurts our ability to compete in the marketplace in originating grain, and it hurts our ability to handle the volume of grain that we should be able to handle through our facility.

Also, that facility is not open to reciprocal switching. If it was, we could originate Conrail grain into that facility. On the eastern seaboard, none of the facilities are open to reciprocal switching. Why? Because the carriers do not wish to compete with one another.

Really, we are talking about competition. That is the issue. If Staggers is going to work and deregulation is going to work, we have to have a competitive rail environment. If we do not, we are going to end up with more regulation in the future, and I do not think anybody on this panel wants to see that happen.

Senator BIDEN. Why are you so sure we are going to end up with more regulation? Are you going to run for the Senate? [Laughter.]

Senator DECONCINI. He is from Baltimore, not Delaware.

Senator BIDEN. I know.

Mr. HARDING. Because there is a lack of a competitive environment.

Senator BIDEN. And you just assume that we will respond to it?

Mr. HARDING. The pendulum has swung too far, it is going to swing back the other way, and I think you will be forced to respond to it by your constituents.

Senator BIDEN. I have no further questions. Thank you.

Senator DECONCINI. Mr. Harding, just to follow up on the Senator from Delaware's question, do you think S. 2417 would give the relief in the specific case that you just cited here as far as competitiveness?

Mr. HARDING. Yes, we do. We do have other issues of concern, such as contract rate disclosure, that are not answered by this bill, but we think it goes a long way in solving our problems.

Senator DECONCINI. Well, thank you, and we hope to hear from various panelists as we proceed down the long road of hopefully enacting some relief in this area. We thank you for your very thoughtful testimony.

Mr. HARDING. Thank you.

Senator DECONCINI. Our next panel will be composed of Ruth Gonze, assistant legislative director, American Public Power Association; Kenneth Holum, general manager, Western Fuels Association, Inc.; Robert Bergland, executive vice president, National Rural Electric Cooperative Association; and Tom Stevenson, the general manager of Western Farmers Electric Cooperative.

Ladies and gentlemen, we have a 5-minute rule here. Your full statements will be printed in the record, and we will start with you, Ms. Gonze.

STATEMENT OF A PANEL CONSISTING OF: RUTH GONZE, ASSISTANT LEGISLATIVE DIRECTOR, AMERICAN PUBLIC POWER ASSOCIATION, WASHINGTON, DC; KENNETH HOLUM, GENERAL MANAGER, WESTERN FUELS ASSOCIATION, INC., WASHINGTON, DC; CAROLYN WATTS, LEGISLATIVE REPRESENTATIVE, NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION, WASHINGTON, DC; AND THOMAS W. STEVENSON, GENERAL MANAGER, WESTERN FARMERS ELECTRIC COOPERATIVE, ANADARKO, OK, ACCOMPANIED BY WALLACE E. BRAND, COUNSEL

Ms. GONZE. Mr. Chairman, Mr. Bergland is not yet here. We are expecting him momentarily.

Senator DECONCINI. OK.

Ms. GONZE. He had another appointment, and in light of his absence, I would suggest that perhaps we might take the other witnesses first and await his appearance. If he does not appear, Carolyn Watts of NRECA staff will present his testimony.

Senator DECONCINI. Carolyn who?

Ms. WATTS. Carolyn Watts.

Senator DECONCINI. Thank you. We will take that suggestion.

Ms. Gonze, please proceed.

Ms. GONZE. Mr. Chairman, my name is Ruth Gonze. I am the assistant legislative director of the American Public Power Association. APPA is the trade association of approximately 1,750 publicly

owned electric utilities, many of which burn coal or buy power made with coal.

We endorse S. 2417 as an effective way to obtain competitive pricing in rail transportation. We do not have such competitive pricing in coal movements now. We have monopoly pricing, which, under the Staggers Act, was to be restrained by the ICC.

But virtually every decision that the ICC has made in every rulemaking since the enactment of the Staggers Act has been a decision for railroad profits—and against consumer protection; 53 percent of our electricity is generated with coal. It is now the usual case for rail transportation to cost one-third to two-thirds of the delivered price of coal. All of that cost is passed through to utility consumers.

This committee is aware that the ICC, in its now infamous 1983 decision, decided that rail rates could rise up to 15 percent a year after inflation. Another so-called constraint on coal rates would stop increases at the stand-alone level, and that is where the shipper could build his own railroad for less money.

The Staggers Act said rates shall be reasonable. Those decisions say the sky is the limit. I would like to take this opportunity, if I may, to read aloud what an ICC administrative law judge said in a case at the Commission, just to show how far the Commission has undermined the Staggers Act. These are his words:

> The bottom line in this proceeding is that the Commission at the present stage of its death throes does not intend, as can be seen from both its actions and inactions, to find a rail rate, no matter how high, to be above a maximum reasonable level.

The operating profit for coal is already 75 percent greater on a per ton basis than for other traffic. Coal revenues have fueled a dramatic financial turnaround for the rail industry. Railroads have amassed billion-dollar war chests to buy unrelated corporations.

How is it that allegedly revenue-inadequate railroads have resources to permit them to buy the El Paso Co. or Texas Gas Resources? But that, Mr. Chairman, is only what we have seen so far. The ICC's 15-percent limit could mean disastrous price increases in this country.

If the railroads take the full 15 percent allowed, then a rate of $12 a ton in 1982 would be $48.50 a ton in 1992. Supposing they do not take that much, and supposing they take only the worst case allowed by the ICC in its environmental impact statement estimate on the impact of the rule. That worst case was a 150-percent increase after 10 years.

In this case, the ICC itself said average electric generation costs nationwide will increase 10 percent by 1990. The impact would, of course, be worse in regions with heavy coal generation. So, in the north central region, generation costs will increase 41 percent annually by 1995. And as drastic as the direct price increases would be, the most damaging effect could be on energy security.

We still import a third of our oil. Twice as much of the gross national product is used to meet energy requirements as was used in 1973. Price hikes have imposed enormous economic penalties on Americans.

National energy policy arose out of those successive price shocks. This policy encourages the use of domestic coal instead of oil. It

does not include a purpose to provide unlimited opportunities for railroads to impose monopoly prices for coal transportation.

But the ICC could wipe out a good portion of the benefit we have achieved in energy security. They could cut coal use by utilities and industry and cut coal exports, while hiking domestic oil and gas use and oil imports.

The ICC's environmental impact statement on its 15-percent-a-year rule tells us how the ICC weighs national energy policy against railroad profits. They actually said this: "With potentially large increases in coal freight rates"—they meant from their rule—"long-distance coal transportation by rail may no longer be economical." Therefore, "within the long-term planning horizon, electric utilities must decide whether previously scheduled coal plants are still economically feasible."

And then they suggested that utilities have three alternatives. They are mine-mouth generation, nuclear power, and wholesale power purchases. That is it, from the ICC, for the Powder River basin and our centuries of coal supply. That cavalierness reflects the bankruptcy of the Interstate Commerce Commission.

It gives the back of the Commission's hand to national energy policy, to American industry, to energy security, and to American consumers. There are only two possible responses to protect the public from the abuses that accompany monopoly power.

The first is effective regulation, but the ICC's record gives shippers scant reason to hope for even-handed regulation without forceful congressional action. The second option is to take steps to restore competition, and within the railroad industry the most effective way to do that is through trackage rights.

Trackage rights would change market structure by letting other carriers or shippers make use of the monopoly railroad facility for a reasonable charge. With access to tracks, captive shippers would have the leverage to negotiate contracts with railroads.

They are not a new concept. Railroads have dealt extensively among themselves to extend such access, but allowing it is now strictly voluntary. It is impossible for shippers to duplicate the existing rail system.

If competition is to be a viable force in much of the rail industry, Congress has to act. S. 2417 would meet that need. We specifically endorse it to inject the benefits of competition in the rail industry. But we would like to emphasize to you that our members view the exercise of trackage rights as a last resort. They are not interested in taking on the business of the railroads. They will only do so if reasonable rates are not available.

But without passage of the bill, captive shippers will not have the leverage to negotiate such rates from monopoly railroads.

We commend you for undertaking this hearing.

[The prepared statement follows:]

STATEMENT
Of
Ruth Gonze
Assistant Legislative Director
AMERICAN PUBLIC POWER ASSOCIATION

before the
Senate Judiciary Committee

On
S. 2417 "The Consumers' Railroad Transportation Antimonopoly Act"

September 18, 1984

My name is Ruth Gonze. I am Assistant Legislative Director of the American Public Power Association (APPA). APPA is the national service organization which represents approximately 1,750 local publicly-owned electric utilities which serve about 14 percent of all U.S. electric consumers.

Because many of our members rely on coal to generate electricity, APPA has a vital interest in matters affecting the rail transportation of coal. We appreciate the opportunity to appear before you this morning and applaud the Committee's interest in examining "trackage rights" as a solution to the problems of captive coal shippers. As the appended policy resolution makes clear, APPA endorses S.2417, the Consumers' Railroad Transportation Antimonopoly Act, as "an effective means for ensuring the benefits of competitive pricing in rail transportation."

The present situation clearly is not providing such protection for the public interest. The Staggers Rail Act of 1980 required that railroad coal rates be reasonable in noncompetitive situations, balancing the need of consumers for affordable energy with the need of railroads for adequate revenues. The Interstate Commerce Commission was charged with the job of balancing those two needs.

But the ICC has not balanced the consumers' interests against the railroads' revenue needs. Coal rate increases lead directly to electric rate increases for consumers -- yet, every decision made by the ICC in every rulemaking since the enactment of the Staggers Act in 1980 has been a decision <u>for</u> railroad profits and <u>against</u> consumer protection.

Fifty-three percent of the nation's electricity is generated with coal. Sixty percent of utility coal is delivered by railroad. Eighty-five percent of the coal shipped by rail is captive to one railroad. It is now the usual case for rail transportation to cost one-third to two-thirds of the delivered price

of coal. Sometimes, transportation costs are almost 80 percent of the delivered price. All of that cost is passed through to utility consumers.

Despite the law's requirement for balance, the ICC, in a now infamous February, 1983, decision, decreed that rail coal rates would be allowed to rise up to fifteen percent per year after inflation. Another "constraint" on rates in that decision would stop increases at the level where the shipper could build his own railroad for less money. The reasoning of the Commission, flawed as it is, seems clear. Through their actions the ICC has communicated that railroads may and should recover any and all revenue shortfalls from a single captive commodity -- coal. And the ICC's direction is in obvious conflict with the stated intent of Congress in the Staggers Act.

In a recent opinion an ICC administrative law judge reached a remarkable conclusion that underscored just how far the Commission has moved in undermining that Congressional intent:

> "The botton line in this proceeding, as well as similar proceedings now before the present Commission, is that the Commission at the present stage of its death throes does not intend, as can be seen from both its actions and inactions, to find a rail rate, no matter how high, to be above a maximum reasonable level. Since that appears to be the Commission's policy, that policy should be followed by the Administrative Law Judges."

Railroads have not hesitated to take advantage of this situation in regard to captive coal shippers. Based on figures available through ICC proceedings, the operating profit for coal is 75 percent greater on a per ton basis that for other traffic. Coal revenues have helped fuel a dramatic financial turnaround for the rail industry. As Robert Long of First Boston has described:

> "...The outlook for the railroad industry remains better than at anytime during the last two decades."

Although the ICC continues to describe all class I railroads as revenue inadequate, Business Week designated the major coal-hauler, Burlington Northern, as a "cash cow," referring to a $1.5 billion war chest, part of which was used to acquire the El Paso Company. CSX, likewise supposedly revenue inadequate, scrimped to accumulate over a billion dollars which allowed them to purchase Texas Gas Resources Company.

The "Value Line Investment Survey" predicted in a 1983 report that "Cyclical recovery of rail traffic, coupled with the heavy operating leverage inherent in railroading, should support big profit gains through 1985-87" for railroads.

These numbers imply profit levels which dictate a policy reaction from regulators. When vast accumulations of capital are obtained through differential pricing, allowed only in consideration of the railroads' claims of desperate need, it is time for regulators to ask: How is it that allegedly revenue-inadequate railroads -- which are allowed rate increases that are not cost-based -- happen to have resources of a magnitude that permit them to buy unrelated billion-dollar corporations?

The fact is that the furthest thing possible from the purposes of the Staggers Act is coal rates set so that railroads can buy natural gas companies.

HOW WILL ICC POLICY AFFECT CONSUMERS?

The ICC's "limit" on rate increases of 15 percent per year after inflation means that real coal rates can double in five years, triple in eight years, and quadruple in 10 years. Price increases of this magnitude would be virtually unprecedented in this country. They would be matched only by price increases for oil imposed by the OPEC international cartel -- and even the price of oil rose no higher in real terms than 15 percent per year from 1973 to 1983.

Rail coal rates have already risen substantially. Since passage of the Railroad Revitalization and Regulatory Reform Act of 1976, when railroads received greater ratemaking autonomy, through 1982, rail coal transport rates increased by 39 percent in constant dollars while coal prices at the mine declined by 20 percent. Now, with the economy coming back strongly there is a fear that railroads will take even greater advantage of the new ratemaking freedoms included in the Staggers Act.

If the railroads take the full 15 percent increase allowed by the ICC -- and indeed do not attempt to go higher, as could happen -- then a rate of $12.02 per ton in 1982 would be $48.59 per ton in 1992.

In its Environmental Impact Statement on the rule permitting 15 percent a year rate increase, [1/] the ICC estimates a "worst case" increase of 150 percent after 10 years. In this case, the ICC itself says, average electricity generation costs nationwide will increase 10 percent by 1990. But the impact

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1/ Ex Parte 347 (Sub. No. 1), "Coal Rate Guidelines - Nationwide," February, 1983.

is much worse in regions with high proportions of coal generation. In the North Central region, generation costs will increase 41 percent annually by 1995, because of the ICC rulemaking. The Central and Midwest regions will experience 16 percent and 10 percent increases respectively by 1995.

Although generation costs are a major expense of electric utilities, they do not represent the total costs of electricity to the consumer. How much, then, will electric bills of the consumer go up in 10 years because of coal freight rate increases? The Consumer Energy Council of America has calculated that, assuming 12 percent annual increases in coal transportation rates (higher than the ICC "worst case," but lower than the ICC allows), the cumulative total transfer of resources over 10 years will be $30 billion, until in the 10th year electric bills will be $7.2 billion higher annually. But again, the impact will be much heavier than the average increase in states with substantial coal generation.

To these numbers must be added the price increases for products and services attributable to electric rate increases, which industry and commercial establishments will pass directly on to consumers.

But coal haul and electric rate increases do not tell the whole story. Significant energy price increases, because they are spread so pervasively throughout the economy, mean reductions in gross national product, higher inflation, more unemployment and extreme hardship for millions of low-income households where one-quarter of income is now devoted to energy costs. Lower coal demand caused by rail rate increases will translate directly into fewer jobs in coal mining, transportation, and industry.

NATIONAL ENERGY POLICY AND COAL RATE INCREASES

Consumers have a vital stake in the success of national energy policy goals. As drastic as the direct price increases mentioned above would be, the most dramatic and damaging effects on the quality of life in this country could result from the failure to achieve energy security.

The United States still imports about one-third of its oil. Twice as much of the gross national product is used to meet energy requirements as was used in 1973. Disruptions in oil supplies and sudden steep price hikes have imposed enormous economic penalties on Americans.

Our present national energy policy arose out of these successive energy price shocks. This policy seeks to encourage the use of coal, an abundant domestic resource, in place of petroleum. Using coal lessens the nation's

vulnerability to energy disruptions from foreign sources.

This policy has been a significant success thus far. Since 1973, 80 percent of the increase in utility generating capacity has been coal-fired. Coal has risen from 42 percent of total generation to 53 percent. The result has been a reduction in oil-fired generation of more than one million barrels per day.

National energy policy has stimulated coal demand to achieve clear purposes. These purposes do not include unfettered opportunities for railroads to impose monopoly pricing for coal transportation. Yet, the regulatory actions of the ICC could wipe out a good part of the benefit we have achieved in energy security. Consumption of coal by utilities and by industry could be depressed, as could coal exports. The upshot would be more domestic oil and natural gas use and higher oil imports.

The ICC's Environmental Impact Statement on its 15 percent per year rule tells us how the ICC weighs national energy policy against coal rate exploitation by railroads. The EIS says, and I quote:

> "With potentially large increases in coal freight rates, long-distance coal transportation by rail may no longer be economical." Therefore, "Within the long-term planning horizon, electric utilities must decide whether previously scheduled coal plants are still economically feasible..."

The ICC suggests that utilities have "basically three alternatives." They are: (1) mine-mouth generation; (2) nuclear power; and (3) wholesale power purchases.

On nuclear power, the ICC notes that coal rate increases of only six percent attributable to its rulemaking will give nuclear power a cost advantage over coal in almost every region of the country.

The Commission also seems to favor large power imports. In fact, the Commission's words suggest that it believes the best thing for many utilities and consumers is just to give up on generating electricity at home. The language of the EIS is astounding:

> "Canada has extensive hydroelectric generating capacity, and it may be more economically feasible for electric utilities to continue to increase the purchase of electric power from Canada rather than to generate that power with either United States coal-fired or nuclear-fired generating facilities. Mexico also has ample domestic energy resources. For many utilities in the Southwest,...it may be more economically attractive to encourage the Mexican utility system to install electric generating equipment so that the domestic electric utilities could purchase that power rather than generate it themselves."

Although there is certainly an important role for imports of energy from Canada and Mexico, the statement I have quoted reflects the total bankruptcy of the Interstate Commerce Commission. It gives the back of the Commission's hand to national energy policy, to American industry, to energy security, and, most of all, to American consumers.

And it means simply this. The current scheme of railroad "regulation" is neither tenable nor tolerable for this country. It means the energy future of this country depends on making new law that will check monopoly profits of railroads.

RESTORING COMPETITION TO THE RAIL TRANSPORT INDUSTRY

There are only two possible responses that will protect the public from the high rates and poor service that seem to inevitably accompany unfettered monopoly. The first is effective regulation, but the record of the current Interstate Commerce Commission gives shippers and consumers scant reason to be hopeful that regulation will become even-handed without strong congressional action to require it.

The second option is to take steps to restore competition, and within the railroad industry one of the most effective way to achieve that objective is through the use of "trackage rights." Trackage rights would change the market structure by allowing other carriers or shippers to make use of a monopoly railroad facility for a reasonable charge. With competing carriers or shippers having access to a track, captive shippers would have the necessary leverage to negotiate more reasonable contracts with railroads.

Trackage rights are not a new concept. Railroads have dealt extensively among themselves to extend such access. The doctrine of "essential facilities" in anti-trust law has been applied to require access to facilities owned by monopolists. It is impossible for shippers to duplicate the existing rail system. If competition is to be a viable force in much of the rail industry, Congress must act.

The extension of trackage rights is now strictly voluntary. Monopolized shippers can expect little relief from trackage rights under the Interstate Commerce Act, because the ICC cannot require extending access to other railroads except in very limited cases and the ICC has no authority to offer trackage rights to shippers.

S. 2417, the Consumers Railroad Transportation Antimonopoly Act, introduced by Senators DeConcini and Baucus would remedy that situation by, as Senator

DeConcini has stated, making it unlawful "for a rail carrier to deny to any shipper the use of a railroad facility which is the sole facility over which such shipper can connect by rail with the trackage of a competing railroad or with a water carrier or can reach the destination of a shipment, when such denial is with the intent to monopolize."

APPA has specifically endorsed S. 2417 as an "effective means for ensuring the benefits of competitive pricing in rail transportation." While we believe the legislation would be a great boon to shippers and consumers we would like to emphasize that our members view the exercise of trackage rights as a last resort. They are not particularly interested in taking on the business of the railroads, but will do so only if competitive rates are not available. Although railroads complain about congestion of rail lines and serious safety problems whenever the concept of trackage rights is raised, they are phantom issues that will never become tangible as long as railroads bargain effectively and offer fair rates. But without passage of S. 2417, captive shippers will not be provided with the leverage to negotiate such rates from monopoly railroads.

Again, APPA commends the Committee for initiating this hearing, and urges your favorable action on the legislation.

"TRACKAGE RIGHTS" FOR CAPTIVE RAIL SHIPPERS

WHEREAS, because 52 percent of electric generation in the United States today is fueled by coal, and 85 percent of all coal shipped by rail is captive to one railroad, the price of electricity is greatly influenced by the costs of rail transportation charged to captive coal shippers, and

WHEREAS, the rate deregulation provisions of the Staggers Rail Act of 1980 were premised on the belief that market competition exists in significant measure and would restrain excessive price increases in large segments of the railroad industry, but this belief is clearly unfounded in many regions, and

WHEREAS, since the enactment of the Staggers Rail Act of 1980, the Interstate Commerce Commission has interpreted the Act in a manner designed to grant railroads virtually unlimited pricing freedom for transporting coal and other captive commodities, despite the Act's intent to continue rail rate regulation where railroads possess monopoly power, and

WHEREAS, in 1983, the American Public Power Association called for legislation to amend the Staggers Rail Act to strengthen essential regulatory protection for captive shippers from monopolistic pricing practices, and

WHEREAS, increased competition in rail services, in addition to effective rate regulation, would greatly benefit captive shippers and consumers through marketplace price discipline, and

WHEREAS, Representative John Seiberling (D-OH) and Senators Dennis DeConcini (D-AZ) and Max Baucus (D-MT) have introduced legislation (H.R. 4559 and S. 2417) to increase rail industry competition by amending the Sherman Antitrust Act to make it unlawful for a rail carrier to deny to any shipper the use of a rail facility which is the sole means by which the shipper can connect by rail with the trackage of a competing rail carrier or reach the destination of a shipment, if such denial is with the intent to monopolize;

NOW, THEREFORE, BE IT RESOLVED: that the American Public Power Association endorses H.R. 4559, the Electric Consumers' Railroad Antimonopoly Act, and S. 2417, the Consumers Railroad Transportation Antimonopoly Act, as effective means for ensuring the benefits of competitive pricing in rail transportation, and also reaffirms its support for legislation to strengthen shipper protections from monopolistic pricing through effective regulation, where railroads continue to exercise monopoly power over the freight transportation of coal and other commodities.

-- Adopted June 12 by the membership of the American Public Power Association at its 1984 Annual Conference in Boston, Massachusetts.

Senator DECONCINI. Thank you, Ms. Gonze, for your testimony. Mr. Holum.

STATEMENT OF KENNETH HOLUM

Mr. HOLUM. Thank you, Mr. Chairman. My name, as you said, is Ken Holum. I am the general manager of Western Fuels Association. I am here this afternoon as the spokesman for Western Fuels Association, incidentally.

I feel compelled at this time because of the experiences I have had in the last hour and a half to make a personal comment. During the decade of the 1969's, I spent a great deal of time in various witness chairs up on Capitol Hill before committees of the House and the Senate.

I developed a hearing problem. I bought a new piece of equipment a month ago and had enough confidence in it that I thought I could volunteer myself as a witness before this committee. I am happy to be here, as I am keenly interested in this legislation. But, I am finding that my new hearing equipment is not working quite as well as I had hoped it would.

Senator DECONCINI. Mr. Holum, that might be very advantageous—you cannot tell with this body—being able to tune in and out some of the rhetoric that goes on. [Laughter.]

But we will take that into consideration and we welcome you here. We know you have a sterling career of testimony on behalf of various different transportation matters, so please proceed.

Mr. HOLUM. I want to say, too, that I think it is quite appropriate that I appear before this committee this afternoon on a panel with the American Public Power Association and the National Rural Electric Cooperative Association. We are members of both of these fine organizations; we support their activities. They have their responsibilities. We are a commercial organization.

Western Fuels is a cooperative whose business is supplying coal at cost to electric generating stations of its consumer-owned members—largely, rural electric generation and transmission cooperatives and municipal electric utilities. I describe our association more fully in my complete statement. I imagine that that will be made a part of the record.

For most of the coal which we supply to our members, we also have arranged for railroad transportation from mine to point of use. Last year, we shipped about 10 million tons of coal, using five different railroads. This year, the total should be higher, so we spend a bit of money with the railroads.

As a consequence, we have gained some reliable, albeit expensive, insights into railroad pricing practices, particularly where one railroad has a monopoly. A monopoly can exist whether or not the ICC determines that the situation meets their market dominance criteria. It is on that basis, partially, that we are here supporting this legislation.

I am pleased to be before you today to present my organization's views on S. 2417, a bill to amend the Sherman Act to prohibit a rail carrier from denying use of an essential facility, a segment of its tracks where certain of its customers are subject to the railroad's monopoly control.

The sponsors of this legislation in both the Senate and the House of Representatives are to be commended for their vision. While many bemoan the absence of regulatory protection and struggle unsuccessfully to reimpose a regulatory framework on the Nation's railroads, the sponsors of this legislation recognize that other legislative mechanisms exist to ensure economic fairness in an area of economic activity crucial to the Nation.

Competition in the railroad industry is an achievable and practical solution to the very serious problems created for captive shippers by the Interstate Commerce Commission's abdication of regulation. It can be accomplished by passage of this simple, easily understood bill, which in no way can be viewed as reregulation.

There is a problem, and it is monopoly. Exacerbating it is the determined resistance of the ICC to apply protections provided by existing statutes for shippers and receivers of bulk products which are limited to a single railroad for transportation service, commonly labeled "captive shippers."

The railroads are a vital link in the Nation's energy supply that we all depend on. We do not advocate anything which would weaken their reasonable financial well-being. But unless their monopoly power is curbed, consumers of electricity will suffer, the coal industry will suffer, and the national energy goals will be unattainable.

In turn, as high freight rates reduce consumption of coal, the railroads themselves will suffer. Unfortunately, Association of American Railroads' spokesmen are stonewalling any suggestion that some changes are necessary. They will tell you that coal prices have gone up more than freight rates. This is not true.

We can buy coal in the Powder River basin in Wyoming today for no more, and in many cases less, than we had to pay 5 or 6 years ago. AAR spokesmen will say that the railroads' rate of return on investment is much lower than that of the investor-owned utilities.

Those utilities, the AAR will neglect to tell you, are fully regulated, being required to justify their expenditures and their rates. Railroads, under current law, are virtually deregulated and are aided by the ICC's lexicon of jargon and mystifying bookkeeping which gives even expert practitioners in the field trouble determining true costs and profits.

When the ICC says railroads can increase their rates 15 percent a year above inflation's increases, they leave the door open to doubling the present rates in 5 years. Human nature being what it is, we know that a monopolist will exercise his monopoly power.

Railroad management could expect to be replaced by the stockholders and board of directors if they did not take all that the law allows in a noncompetitive situation. Andrew Carnegie, the eminent steel tycoon of the last century, located new steel mills where there were two railroads and possibly a navigable river.

His biographer noted that:

> Carnegie, an experienced rate-maker himself, knew only too well what to expect should he locate his works where one railroad had a monopoly—extortion.

Passage of S. 2417 would reduce the opportunities for extortion. I think it merits very careful consideration by this committee and

the Congress, and I appreciate the opportunity to sit before you and support it.

Thank you, Mr. Chairman.

[The prepared statement follows:]

TESTIMONY ON S. 2417

OF

KENNETH HOLUM
GENERAL MANAGER
WESTERN FUELS ASSOCIATION, INC.

MR. CHAIRMAN. My name is Ken Holum. I am general manager of Western Fuels Association, Inc., a cooperative, non-profit organization whose business is supplying coal to the electric generating stations of its consumer-owned members -- largely rural electric generation and transmission cooperatives and municipal utilities. I describe our Association more fully in an appendix to my testimony.

For most of the coal which we supply to our members, we also arranged for railroad transportation from mines to points of use. Last year, we shipped about 10 million tons of coal. It was delivered over five railroads. This year, the total should be higher. As you can imagine, we spend quite a bit of money with the railroads. As a consequence, we have gained some reliable -- albeit expensive -- insights into railroad pricing practices, particularly where one railroad has a monopoly. It is on that basis, partially, that we are supporting this legislation.

I am pleased to be before you today to present the views of my organization on S. 2147, a bill to amend the Sherman Act to prohibit a rail carrier from denying use of an essential facility -- a portion of its tracks -- where certain of its customers are subject to the railroad's monopoly control.

The sponsors of this legislation in the Senate and similar legislation in the House of Representatives are to be commended for their vision. While many bemoan the absence of regulatory protection and struggle unsuccessfully to reimpose a regulatory

framework on the nation's railroads, the sponsors of this legislation recognize that other legislative mechanisms exist to ensure economic fairness in an area of economic activity crucial to the nation. They have found the answer in the American free enterprise tradition -- competition.

There is a major problem in the field of rail transportation. It is unregulated monopoly. As more and more mergers occur, there will be more monopoly and less competition. Shippers of bulk products throughout the United States (with only rare exception) testify that they have to cope with unfairly high, or unnecessarily high, freight rates because of monopoly. The rash of bills and joint resolutions which have been introduced during the 98th Congress attest to the truth of this statement, as do recurrent articles in the coal and transportation trade press. For example:

> -- "Rail Costs Held Depressing Foreign Mart for US Coal" (Journal of Commerce, November 28, 1983)
>
> -- "Transportation Costs are Biggest Barrier to Western Coal Growth, Analyst Says" (Coal Outlook, June 18, 1984)
>
> -- "ICC Railroad Coal Rate Guidelines Will Hurt Coal Production, EIA Study Says" (Coal News, August 22, 1983 -- EIA being the Dept. of Energy's Energy Information Adminis.)
>
> -- "Shippers Are Wasting Time Seeking Relief at ICC, Says Administrative Law Judge" (Coal Transportation Report, February 6, 1984)
>
> -- "Study Says Rail Rates Cost Wyoming 10 Million T/Y" (Western Coal, July 5, 1984)
>
> -- "Colorado Coal Losing Market Share" (Coal Outlook, September 10, 1984 -- with this article stating that transportation costs are the chief cause of the loss)

Exacerbating monopoly is the determined resistance of the Interstate Commerce Commission (ICC) to apply protections provided by existing statutes for shippers and receivers of bulk products which are limited to a single railroad for transportation service. These are commonly labeled "captive shippers" or users of "captive traffic". The Staggers Rail Act

of 1980 made restoring railroads to fiscal health one of its main goals. Another equally important goal, as stated in the Act, is "maintaining reasonable rates where there is an absence of effective competition...". The ICC diligently pursues the goal related to financial health of the railroads while ignoring its obligation to maintain reasonable rates where real, viable competition does not exist.

Since the enactment of the Staggers Act, the ICC has not found one instance -- not one -- where a railroad is charging a captive shipper an unreasonable rate. Does anyone believe that the nation's railroads are that charitable?

Competition in the railroad industry is an achievable and practical solution to the very serious problems created by the ICC's abdication of regulation in behalf of captive shippers -- of coal, ore, grain, forest products, chemicals, fertilizers, and almost any other bulk product. The goal of achieving competition can be accomplished by passage of this simple, easily understood bill -- a bill which in no way can be viewed as re-regulation.

As a matter of fact, most approaches to correcting the existing problems either call for some measure of re-regulation or give additional duties to an ICC which has shown that it doesn't care to be involved and no longer looks after the interests of consumers.

The bill we are discussing today leaves regulation or deregulation where it is at present. If there is a need to amend the Staggers Act (and many believe that changes are needed) that is for other Committees and other times. We believe that competition will solve most of the problems we are discussing and that this bill will create competition where monopoly now exists.

Western Fuels is a Wyoming corporation. Although our membership is nationwide and we have business relationships in many states, a major portion of the coal we buy from others originates in nat state. Wyoming is one of the nation's coal rich states and coal is a resource critical to the nation's energy needs.

Three railroads have trackage in Wyoming. Two of the three have exclusive access to two of the state's major coal producing areas. The third holds a competitive position with respect to a limited number of mines. The three railroads serving Wyoming all interconnect and extend to different potential delivery points over a wide geographic area.

If and when S. 2417 becomes law, all three carriers will be able to compete for coal related business originating at all Wyoming mines. If the railroad winning the business in an open competitive market does not have direct access to the mine supplying the coal, it would use the tracks of its competitors to reach its own lines. The winning carrier would, of course, be obligated to pay a fair and reasonable charge for the use of the other carrier's trackage.

We have stated that there is a problem -- monopoly, and that there is a solution, enactment of this bill. But, some might ask, is it <u>that</u> big a problem? Yes, and it will become bigger as more coal is burned by more utilities to meet the nation's need for electricity. At present, about 55% of the electricity used in this country is produced from coal. Shippers and users of that coal are limited to one railroad for about 70% of the tonnage moved. This is the true "captive shipper" situation.

Delivery of fuel for use in this vital industry by these monopolies ;is a costly and major problem. We must change this to a competitive situation.

We believe that coal producers, coal users, electric utility customers, and the public generally would benefit. Competition would hold down the constantly increasing freight rates which have been the norm. And, in the end, by making coal more economical, demand would increase and the railroads also would benefit.

The railroads are a vital link in the nation's energy supply. We all depend upon them. Western Fuels does not advocate anything which would weaken the railroads' reasonable financial well being. We want, and need, an economically viable well-managed railroad system. This goal can be achieved in an American free enterprise competitive environment while protecting the interests of captive shippers. Unless we maintain a proper and reasonable balance, electric consumers, the coal industry, and our export markets will all suffer and we will become more, rather than less, dependent upon imported oil.

Unfortunately, the American Association of Railroads (AAR) - spokesmen for the railroad industry -- is stonewalling any suggestion that some changes are necessary. Its spokesmen deny that much coal is in the captive traffic situation and instead suggest that a power plant designed to burn a certain kind of coal can shift to a different fuel, or get its coal from overseas. The ICC so far has backed them up on this.

The AAR will tell you that coal prices have gone up more than freight rates. This is not true. We can buy coal in the Powder River Basin of Wyoming today for no more (and in many cases less) than we had to pay five or six years ago.

AAR's spokesmen will say that the railroads' rate of return on investment is much lower than that of investor-owned utilities. Those utilities, the AAR will neglect to tell you, are fully regulated and are required to justify their expenditures and their rates. Railroads, under current law, are

virtually deregulated and are aided by the ICC's lexicon of jargon and mystifying bookkeeping. Both give even expert practitioners in the field trouble determining true costs and profits.

A dim view of the ICC's accounting methods was provided in a report completed earlier this year entitled "Railroad Revenue Adequacy: A Critical Analysis". Produced by Multinational Business Services, Inc. - which is headed by Jim Tozzi, a respected Washington economist - the report states, in part, that the ICC

> ...determines revenue adequacy by calculating return on investment. But the ICC allows accounting methods that understate (railroad) income, overstate investment base, and maximize the true cost of capital.

Under current regulatory law, as interpreted by the ICC, until a railroad becomes revenue adequate it has great freedom to increase freight rates annually. At present, not a single Class 1 railroad is "revenue adequate" nor, under the conditions cited in the Tozzi report, are any likely to become so. Yet, they are able to acquire other large corporations -- as has been the case during the last year or so -- with their inadequate income.

Not only do independent analysts find the ICC's methods and procedures questionable, employees of the agency do also.

In a matter considered by the ICC, the decision of which was announced on January 18, 1984, Administrative Law Judge James E. Hopkins of the ICC stated that it was his view

> ...that complainants are wasting an enormous amount of time, energy, and money proceeding with these cases before a Commission that has clearly shown that it is unable or unwilling to find a complained of rail rate to be above a maximum reasonable level where a carrier is not revenue adequate.

He continued that while what goes into deciding the revenue

adequacy issue is another matter, the way the ICC is construing the Staggers Rail Act of 1980, even on an interim basis, "leaves no hope for complainant shippers".

When the ICC says railroads can increase their rates 15% per year above inflation's increases, they leave the door open to doubling of present rates in five years. Human nature being what it is, we know that a monopolist will exercise its monopoly power. Railroad management could expect to be replaced by the stockholders and boards of directors if they did not take all the law allows in noncompetitive situations.

Our experiences with the many railroads with whom we have dealt has varied. But there is one constant. Where true competition exists, where we have economic leverage, where a railroad wants our business, the railroads have invariably been responsive to our concerns for price, terms, service commitments, and the like. Negotiating with railroads can be a pleasant experience.

Unfortunately, the opposite is also true.

A shipper's primary concern is price related. In connection with certain of our activities over the past few years, we have had occasion to consider the impact of competition on railroad pricing. We have also commissioned expert studies of the price level one might expect for moving coal in a competitive environment versus a non-competitive environment.

One of Western Fuels' consultants -- Gerald W. Fauth, a noted railroad cost expert -- is of the opinion that a conservative estimate of a competitive rate would produce a ratio of revenue to variable cost of 150%. This is well below the level of ICC theoretical involvement under the Staggers Act.

Mr. Fauth, with the help of tariff files maintained by the

Tennessee Valley Authority, has also done a comparison of non-competitive rates with rates responsive to barge competition. This comparison shows competitive rates 44.9% lower than non-competitive rates.

There really can be no argument over the benefits of competition, both with respect to rates and to performance. We support the current legislation precisely for that reason. It is pro-competitive. It does not involve re-regulation of the nation's railroads. If enacted, it must ultimately lead to benefits for both shippers and railroads.

Nearly 200 years ago, the English economist Adam Smith called competition "the lifeblood of efficient economic performance". We believe this is still acceptable doctrine in the United States.

Competition remains a possibility where two railroads serve the same area. It is not a possibility under ICC interpretations where a mine, or a grain elevator, or a sawmill, or other producers of bulk products have only one railroad to turn to. As I noted earlier, the ICC has a language all its own and can develop meanings and definitions that utterly surprise those involved. Such terms as "revenue adequacy", "stand alone costing", "market dominance", and "revenue to variable cost ratio" can take on meanings all their own at the Commission. With no place else to go, a shipper starts out at a disadvantage to the railroads.

Even if the ICC were still regulating rates, there remains the large problem created by the very structure of the Staggers Act. It precludes rate reasonableness review by the ICC where rates are below 170% of variable cost. Above that level the ICC has discretion as the whether or not to intervene. We know from the record that rates at that level produce monopoly profits.

Fortunately for us all, there is a simple alternative. We

can forget the special language and meanings used by the ICC in the areas I have discussed today where captive shippers at present have no recourse. That alternative is enactment of the bill we are discussing. It can become a self-enforcing directive against monopoly, giving true competition a needed boost.

In 1873, Andrew Carnegie, the eminent steel tycoon, was locating a new steel mill in western Pennsylvania. Following his practice, he had his aides locate a site where there would be service by two railroads, as well as a river for water transport. His biographer, Harold C. Livesay, noted that:

> "Carnegie, an experienced rate-maker himself, knew only too well what to expect should he locate his works where one railroad had a monopoly -- extortion."

Passage of S. 2417 would reduce the opportunities for extortion.

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As an appendix to my testimony, I would like at this point to tell you more about Western Fuels Association, Inc., and our experiences in the coal transportation marketplace.

Western Fuels celebrated its 10th anniversary in July of this year. Originally founded by two rural electric generation and transmission (G&T) cooperatives to secure fuel for use in new electric generation facilites, we now have more than 30 members stretching from California to Puerto Rico and from Canada to Mexico. In 1983, our coal sales to members exceeded $200 million for the first time. Western Fuels is truly a national energy supply cooperative, and it is unique.

Western Fuels Association's member-owners are rural electric cooperatives, municipal electric utilities, and public power districts. Our executive offices are in Washington, DC, and our technical and developmental offices in Denver, Colorado.

Under most contracts with our members, the coal sale is made at the point of delivery. This means we are directly involved in the transportation of coal.

Coal for member use is acquired in one of two ways: we either buy coal from other producers or we acquire coal in the ground and finance, build, and operate mines.

Western Fuels has negotiated contracts for over 250 million tons of coal to be delivered from five Powder River Basin area mines to members power plants in Wyoming, Louisiana, and Kansas. Until recently, all Power River Basin coal originated on the Burlington-Northern's lines. Most of it still does. The Missouri Pacific and the Santa Fe are connecting carriers on two of the three Powder River Basin movements.

Western Fuels owns two underground coal mines -- one in Colorado and the other in Illinois. The Colorado coal will be delivered to a member power plant in Utah via a 35-mile electrified railroad known as the Deseret-Western Railway, which is owned and operated by Western Fuels.

The Illinois coal is located along the Illinois Central Gulf Railroad and is delivered to member power plants in Kansas and Missouri. The Missouri Pacific Railroad is a connecting carrier for the Missouri deliveries.

In New Mexico, Western Fuels is involved in a joint venture with affiliated companies of Santa Fe Industries for coal delivered to a member power plant. We initially contemplated delivering this coal via a movement on the Santa Fe Railroad

main line. However, due to the proximity of the mine to the power plant, we have been able to structure a delivery system involving four miles of new connector track. The rail delivery system will be known as the Escalante-Western Railway and will be owned by Western Fuels.

As you can see, we deal with many railroads. In addition, given our involvement in two of our own separate rail delivery systems, we believe we have a good understanding of railroad costs.

While we have been involved in some very visible arguments with railroads, I am able to say today that we either have -- or hope to have amicable relationships with all with whom we do business. We have been successful in developing these relationships without the involvement of the Interstate Commerce Commission.

Our success should not be interpreted to mean no problems exist. Rather, our success argues for the legislative approach embodied by S. 2417.

Senator DECONCINI. Mr. Holum, thank you very much for your testimony.

Next, we will hear from Mr. Stevenson.

STATEMENT OF CAROLYN WATTS

Ms. WATTS. Actually, Mr. Chairman, if you do not mind, I would prefer to introduce Mr. Stevenson.

Senator DECONCINI. Sure. Please proceed.

Ms. WATTS. My name is Carolyn Herr Watts and I am the legislative representative for the National Rural Electric Cooperative Association. NRECA is the national service organization of more than 1,000 consumer-owned, not-for-profit electric systems serving 25 million consumers.

I am pleased to appear today in support of S. 2417. The membership of NRECA has expressed its support of this legislation by the policy resolution which is attached to our full testimony.

Our cooperative members feel quite strongly about the issue of monopolized rail shipments. Coal is an important element in the rural electric fuel mix, as 72 percent of our own generating capacity is coal-fired. This amounts to more than 14,000 megawatts.

Today, I am pleased to be accompanied by Mr. Tom Stevenson, who is the manager of Western Farmers Electric Cooperative in Anadarko, OK.

Mr. Stevenson.

[The prepared statement follows:]

TESTIMONY OF BOB BERGLAND

Executive Vice President of the

National Rural Electric Cooperative Association

before the Senate Committee on the Judiciary

on S. 2417

September 18, 1984

Mr. Chairman, my name is Bob Bergland. I am Executive Vice President of the National Rural Electric Cooperative Association (NRECA). NRECA is the national service organization of more than 1,000 consumer-owned, not-for-profit electric systems serving 25 million consumers in the sparsely-populated areas of 46 states.

I am accompanied here today by Mr. Tom Stephenson, Manager, Western Farmers Electric Co-op, Anadarko, Oklahoma. Mr. Stephenson will be presenting testimony concerning Western Farmer's attempts to aquire trackage rights from the Burlington Northern Railroad.

I am pleased to appear today in support of S. 2417, which would amend the Sherman Act to require one rail carrier to permit other rail carriers, or shippers, to use its tracks at reasonable costs to transport certain goods. Refusal to do so would constitute a violation of the antitrust laws.

The membership of NRECA has expressed its support of such legislation in the following policy resolution endorsed by more than 8,000 members at the 42nd Annual Meeting in January 1984:

RAIL TRANSPORTATION TARIFFS

The Congress has enacted the Staggers Railroad Act which substantially penalized captive shippers such as coal-burning electric utilities and grain producers. The Interstate Commerce Commission (ICC) has adopted the theory that railroads should be free to establish tariffs in excess of fully allocated costs for captive shippers as a means of compensating railroads for the movement of other commodities. As a result of this shift from the traditional ratemaking criteria, based upon actual cost of service, the electric consumers are being required to pay through electric rates for unjustifiable increases in the cost of transportation. These increases can cause present rates to double within five years.

Our efforts to work with the appropriate coal transportation organizations, Congress and the ICC to reverse its punitive and unreasonable ratemaking philosophy have so far proved unsuccessful. We continue to believe that rates charged for the movement of coal should allow a reasonable rate of return to the railroads, based upon actual cost of service, but should not be allowed to become a means of subsidization of other railroad traffic.

We encourage the ICC to recognize the captive nature of utility coal movements and to protect coal users against monopolistic pricing practices on the part of railroads.

> Further, we vigorously support legislative efforts to provide relief for captive shippers such as H.R. 2584 and S. 1082 which would amend and clarify the Staggers Act and H.R. 4559 amending the Sherman Antitrust Act to provide competitive pricing through granting captive shippers and the railroads access to limited stretches of trackage owned and controlled by a monopoly railroad.

(This resolution was adopted prior to the introduction of S. 2417, otherwise it would have also referenced S. 2417.)

Our cooperative members feel strongly about the issue of monopolized coal shipments. Coal is an important element in the rural electric fuel mix as 72% of our generating capacity is coal-fired (14,625 MW).

Currently many electric cooperative generating stations are "captive" to a single rail carrier. In these situations, one railroad has total control over coal movements from the mine to the powerplant. The Staggers Rail Act of 1980 substantially deregulated the rail industry. We do not quarrel with the goals of the Staggers Act which were to improve the financial health of the railroads while simulataneously providing protection for captive shippers. However, these monopolized shippers, which include the electrical generation cooperative members of NRECA, have not received the promised captive shipper protection under the Interstate Commerce Commission's interpretation of the Staggers Rail Act. ICC holdings permit railroads to raise freight rates on coal by 15% per year over inflation; thus doubling such rates over five years. Our major concern centers on shippers without any other transportation alternative.

Competition is the focus of S. 2417. It provides that a shipper or other railroad can compete for the shipment of coal by using the tracks of the monopoly railroad. We do not necessarily want to be in the railroad business, but we want to bring our member-consumers the most reasonably priced electricity possible even if that means running our own trains. When we enter into negotiations with a rail carrier, we want to sit down with equal standing. What is negotiation if there is not an alternative to which one could turn given unfavorable rail rates? Most rural electric systems own their own rail cars because of the railroad companies' insistence, thus the railroads have already thrust us partly into the rail business. .If they cannot or will not provide reasonable service for reasonable fees we should be given the opportunity to do the job ourselves.

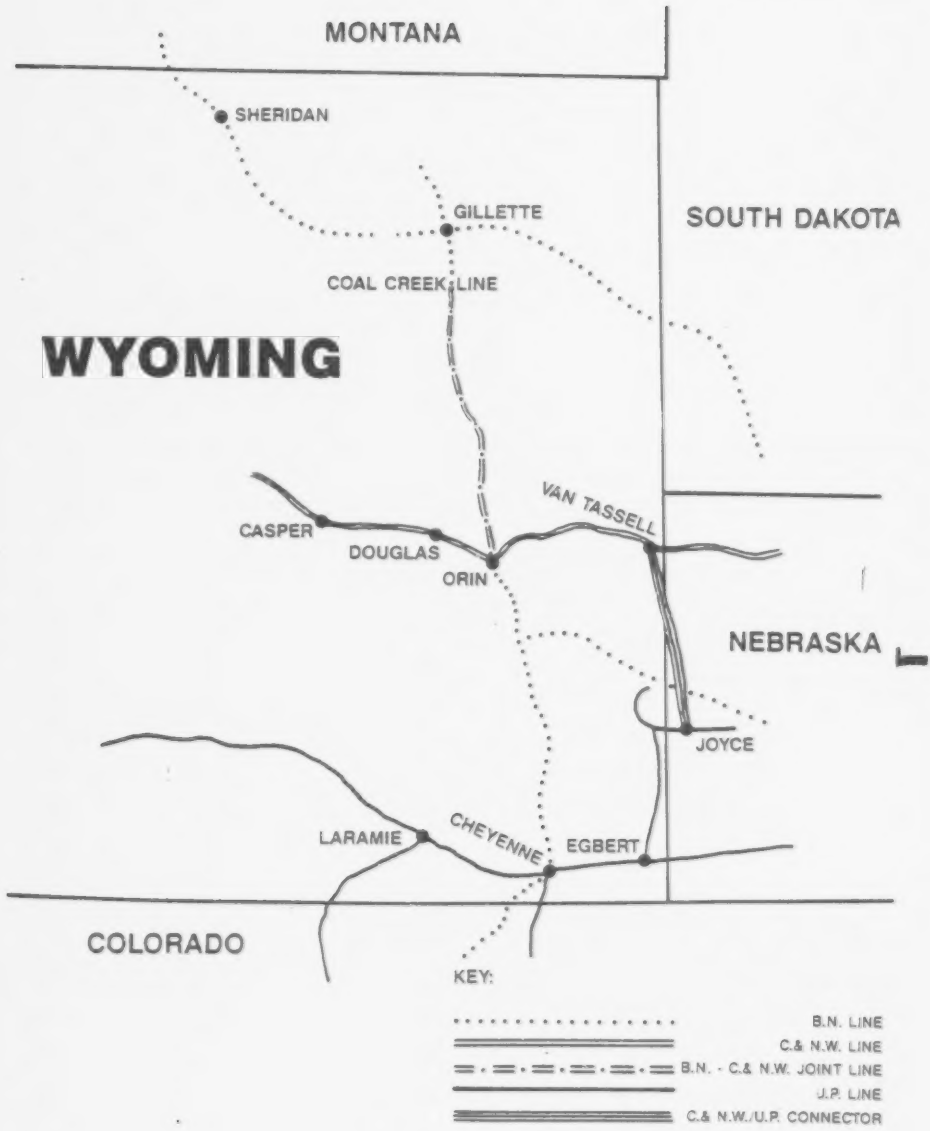
S. 2417, Mr. Chairman, will provide both competition and a yardstick by which to measure the true cost of providing rail service. By creating a

competitive environment we will, in turn, create increasing efficiencies of service. Competition will shape the marketplace. In my opinion, the granting of access to tracks is a lever, a last resort, if you will, to encourage effective on-going bargaining between the rail carrier and the shipper.

NRECA supports the market ratemaking approach to rail rates as embodied in S. 2417. The Interstate Commerce Commission has placed a heavy reliance upon negotiated rail rates. This reliance assumes that a utility has sufficient bargaining leverage to negotiate reasonable rates. Some of our member cooperatives have worked out very favorable rail rates. For example, Arkansas Electric Co-op Corporation, which is in partnership with Arkansas Power & Light Company, has signed a contract with the Chicago & Northwestern-Union Pacific railroads after a three-way competition with the Burlington Northern and the proposed ETSI coal slurry pipeline. Cajun Electric Power Co-op, Inc of Baton Rouge, Louisiana, using similar bargaining strategy, recently signed a long-term contract with the Burlington Northern. We are very proud of these successful contracts, but they are a minority and the key to their success was competition.

I have attached to this statement a map of the Powder River Basin coal region. It is evident from the graphic display that rail competition exists in only specific areas. North of the Coal Creek line, only one rail carrier exists. The enactment of S. 2417 would open up the entire area to competition among carriers. I have also attached an NRECA brochure entitled RAIL RATES/Non-Competitive developed for use at the NRECA Legislative Conference held in May of this year.

In summary, Mr. Chairman, NRECA and its member systems heartily endorse S. 2417. We prefer this free-market, competitive approach to ensure fair and reasonable rail tariffs. We have no real desire to enter the rail business ourselves, but the use of the antitrust law, as embodied in S. 2417, would afford our member cooperatives the means to negotiate reasonable rates with existing carriers. I thank you for this opportunity to testify.


MONTANA
SHERIDAN
GILLETTE
SOUTH DAKOTA
COAL CREEK LINE
WYOMING
VAN TASSELL
CASPER
DOUGLAS
ORIN
NEBRASKA
JOYCE
LARAMIE
CHEYENNE
EGBERT
COLORADO
KEY:
B.N. LINE
C.& N.W. LINE
B.N. - C.& N.W. JOINT LINE
U.P. LINE
C.& N.W./U.P. CONNECTOR

STATEMENT OF THOMAS W. STEVENSON

Mr. STEVENSON. Mr. Chairman, members of the committee, I am Tom Stevenson, manager of Western Farmers Electric Cooperative of Anadarko, OK. I am accompanied today by Wallace Brand, our attorney.

Western Farmers is a generation and transmission cooperative. Our business is supplying electric power to distribution cooperatives who serve approximately 460,000 people in rural Oklahoma.

I believe that the committee has been furnished copies of my prepared testimony and I will not repeat all the points here. I would like to summarize our situation very briefly and then answer any questions that you might have.

In 1977, we needed to add generation to meet our growing load. The Federal Government urged us to shift from gas to coal as our fuel for new generation, so we started building a coal-fired unit at Fort Towson in Oklahoma, and we found a low-sulfur coal supply in the Powder River basin.

When we signed our coal contract with the mine, the railroads quoted us $11.94 a ton for transportation. Our current rate today is $23.69.

Senator DECONCINI. What span of years is that?

Mr. STEVENSON. 1977.

Senator DECONCINI. Thank you.

Mr. STEVENSON. Then, of course, in 1980 the Congress passed the Staggers Act. In 1981, when we actually began operating our new plant, the Burlington Northern started charging us in accordance with the supply and demand.

Unfortunately, there was plenty of demand and only one supplier, and the Burlington Northern's price reflected this situation. As I stated before, we are now paying twice what we were quoted in 1977.

Another form of transportation we might have used was a coal slurry line, but it got knocked out by the railroads' group boycott. They all refused the permission to cross their tracks.

While the pipeline finally got all the rights-of-way, the delay was very effective and added expense ultimately that put it out of the market. I understand that a grand jury is looking into that issue.

Coal transportation is two-thirds of our coal fuel cost. The railroads' monopoly prices are tearing our cooperative apart. They are threatening our ability to continue to serve our customers.

In this situation, the only way we can get competition is to enter the coal transportation business ourselves, or at least have the right to enter it. The only practical way to enter is through trackage rights because no individual shipper can possibly afford to build his own tracks over any distance.

The right to enter might be enough because the railroad would then have to take that possibility into account when they quote us their transportation rates.

We asked the Burlington Northern for trackage rights. They turned us down for two reasons that are completely spurious, as you can see for yourselves in the correspondence attached to my prepared testimony.

Of course, we can sue them for violating the antitrust laws. But under the law as it now stands, it would take many years and millions of dollars in litigation expenses to pursue our claim.

We understand this legislation would make a refusal to grant trackage rights a per se violation of the antitrust laws. We believe that this will give us a realistic chance to help ourselves get out from underneath the Burlington Northern's monopoly.

If you have any questions, we will be glad to answer them.

[The prepared statement follows:]

43-746 O - 85 - 6

TESTIMONY OF
THOMAS W. STEVENSON, GENERAL MANAGER
OF WESTERN FARMERS ELECTRIC COOPERATIVE
ON S. 2417

I am Thomas W. Stevenson, General Manager of Western Farmers Electric Cooperative. We are a generation and transmission electric cooperative headquartered in Anadarko, Oklahoma. We supply electric power in bulk to our member distribution cooperatives which in turn serve approximately 460,000 rural electric consumers in our state. Fuel for generation is our largest budget item, and transportation accounts for two-thirds of the cost of our coal, which is our base load fuel. We own 3 unit trains of 100 railcars each (and 30 reserve cars) which we use to move coal from the Powder River Basin in Wyoming to our primary generating facility, the coal-fired Hugo generating plant located near Ft. Towson in southeastern Oklahoma. We are captive to the Burlington Northern Railroad in obtaining rail transportation for that movement, and this circumstance has seriously affected our viability as an electric utility.

We are the Burlington Northern's captive customer today because, back in 1977, prior to the Staggers Act, we made two key decisions. We entered into a long term contract with Shell Oil Company to buy the coal supply for our planned new generating plant from its Buckskin mine north of Gillette, Wyoming, and, at the same time, we decided to construct the new plant on a site near Ft. Towson.

Until just this month, the Burlington Northern has had a complete monopoly of coal traffic originating in the entire Powder River Basin. One other railroad, the Chicago and Northwestern, is now able to begin sharing in the portion of that traffic south of Coal Creek Junction. There is but a single exception, however, to the Burlington Northern's continuing monopoly north of Coal Creek Junction. One mine located just north of that point obtained the right to build a short spur south to reach the Chicago and Northwestern by bringing and settling an antitrust suit against the Burlington Northern and the Chicago and Northwestern based on a per se violation of the antitrust laws.

Shell's Buckskin mine is about 50 miles north of Coal Creek Junction. We tried to put together a group of coal shippers and mines to build track to bridge the gap. We soon concluded, based on the attitude of the Chicago and Northwestern toward the project, that we weren't going to get much more competition out of the duopoly than we have from the monopoly. The lack of cooperation of the Chicago and Northwestern killed our project.

On the southern end of our haul we are also captive to the Burlington Northern between Durant, Oklahoma, and Ft. Towson.

In October, 1977, after a lot of shopping around and studying we decided to buy our coal from Shell's mine. We relied on a quote of $11.94 per ton to transport the coal by rail to Oklahoma. This was before the Staggers Act, when we thought we could count on ICC rate regulation to protect us. The Frisco gave us the rate quote and told us the Burlington Northern supported it. Since then those two railroads have merged. Now we pay $23.69 per ton -- about double what was quoted to us in 1977 and twice what we pay for the coal itself.

In the spring of 1983, our rail consultants advised us that we could save as much as $500 million over the next 8 years by providing our own coal transportation. They estimated the savings by comparing the cost of our leasing trackage rights and operating our own trains with the anticipated charges of the Burlington Northern applying the ICC's Ex Parte 347 guidelines.

By letter of April 4, 1983, we asked the Burlington Northern to lease us trackage rights. They turned us down a couple months later for reasons we think are completely spurious. They told us they were not permitted by law to lease trackage rights to a shipper. They also claimed we would not save any money, but they admitted they had made no study of the matter. As I mentioned earlier, our consultants' study showed substantial savings. (I have attached copies of our correspondence on this subject to my testimony as Exhibit No. 1.)

Our attorneys advise us that this refusal to deal is actionable under Section 2 of the Sherman Act as an unreasonable refusal to grant use of an essential facility. (They have

recently published an article on this question in the trade press, and I have attached a copy to my testimony as Exhibit No. 2.) However, they also tell us that trying the unreasonableness of particular conduct to a court under Section 2 is very difficult and time consuming. The costs of such litigation, they say, might ultimately be as much as one or two million dollars or more, and the case might take five to seven years or even longer before ultimate resolution.

As we understand your bill, it would make a refusal to grant trackage rights to a captive shipper a "per se" antitrust violation, so we would not have to spend so much time and treasure to get relief.

We have sought help from the ICC, but under the present law no real rate relief is available and it takes years even to get a decision. We would like to obtain rights to trackage so that we can help ourselves. We believe if we had that option to escape from monopoly pricing it would put an effective ceiling on the railroad's price even if we didn't actually start hauling coal ourselves.

We have been trying to bargain for a rail transportation contract with the Burlington Northern, but they have candidly stated that they take our lack of alternatives into consideration in setting their price. We proposed a contract that would let them keep half of their monopoly profits from serving us, but their response was to offer only a small price reduction -- less than 5 percent.

Shell Oil wrote into our coal contract a provision excusing performance should either party be prevented from performing because of inability to acquire essential rail transportation at a reasonable cost. We believe this excused performance clause may free us from the Burlington Northern's monopoly at the northern end. We recently notified Shell, as the contract requires, that we anticipated our performance would be prevented for this reason. Shell told us that it didn't agree with our interpretation of the contract and, without even sitting down to discuss the matter with us as we had invited, promptly filed suit in the Wyoming Federal District Court. (I have attached the

relevant correspondence with Shell to my testimony as Exhibit No. 3.)

Our attorneys advise us that we had best avoid further discussion of this matter because it is pending trial, but I thought you should know at least that, if the Wyoming Court decides in our favor, we might escape captivity on the northern end of our movement.

On the southern end, as I mentioned earlier, we are captive for almost the last 60 miles to Ft. Towson. A ballpark estimate of our cost to construct a spur for 60 miles is about $60 million, if no special difficulty is involved. That's a lot of money for a small cooperative. This assumes also that we would be able to obtain the necessary permits and envi mental approvals to build such a duplicate line. We may also have an opportunity to buy some existing track coming in to the plant from another direction, but that would make us dependent on a railroad that has been mentioned as another possible acquisition by the Burlington Northern.

The Burlington Northern could not be described as one of the sick railroads the Staggers Act intended to protect. It has been referred to in the meetings of the financial analysts in New York as a "cash cow." With its enormous earnings on coal hauling, it has bought up the giant El Paso Natural Gas Company. The Burlington Northern exercises virtually unchallenged monopoly power. This bill would help provide for effective competition by a shipper like us served by such a monopoly railroad. It would ensure the free market competitive system that Congress had in mind when it passed the Staggers Act and terminated the ICC's strict review of railroad pricing.

Thank you for the opportunity to appear before you today. I will be pleased to answer any questions.

EXHIBIT NO. 1

Western Farmers' Correspondence with
Burlington Northern Railroad Concerning
Request for Trackage Rights

Western Farmers Electric Cooperative
P. O. DRAWER 429 -:- PHONE 247-3351
ANADARKO, OKLAHOMA 73005

April 4, 1983

Mr. Gus Cobb
Burlington Northern
176 East Fifth Street
St. Paul, Minnesota 55101

Dear Mr. Cobb:

As a consumer-owned electric utility, Western Farmers is especially concerned with the increasing price of electric power to its members in this inflationary time. We are continually looking for ways to operate more efficiently and keep our costs as low as possible for their benefit.

A significant part of our cost of service is the supply of coal for generation at our new Hugo Plant--particularly the transportation of that coal from our source in Wyoming to the plant. You know from our litigation at the I.C.C. on your tariff how concerned we are about this constantly rising cost.

To obtain more control over this important cost factor, Western Farmers is exploring the feasibility of transporting the coal itself instead of purchasing the transportation service. As you know, we have already invested in the 330 hopper cars used for the unit train movement over your system. We believe we can acquire the necessary motive power and can employ the train crews. It is possible that we may save substantial sums on labor costs. Of course, the key to our operating a coal transportation business would be obtaining the right to use your tracks for the movement, since it would be impossible for us to duplicate them. Would Burlington Northern lease Western Farmers' trackage rights from the Buckskin mine to the Hugo Plant for this purpose?

We would appreciate the opportunity to discuss with you the appropriate price and terms for such a lease.

Sincerely,

Marvin Scherler
President

COPY

Leon

BURLINGTON NORTHERN RAILROAD

O.W. COBB
Vice President
Coal & Taconite Pricing

176 East Fifth Street
St. Paul, Minnesota 55101

Mr. Marvin Scherler
President
Western Farmers Electric Cooperative
P. O. Box 429
Anadarko, Oklahoma 73005

June 2, 1983

Dear Mr. Scherler:

We have been considering your proposed approach to the transportation of coal from Wyoming to your Hugo plant at Ft. Towson as outlined in your letter of April 4, 1983, and believe we are without power to grant an individual shipper the kind of rights you seek. We also believe that your hope of possibly reduced transportation costs would not be fulfilled.

Even if the regulatory obstacles could be overcome, which we doubt, and you were ultimately authorized to transport coal for yourself, albeit at considerably greater cost than your rates, we beliive the novel approach you suggest would take considerable time to pursue. We would like to resolve our differences more rapidly than would thereby be required. If you have any further views how this might be accomplished, we would be pleased to hear from you.

Very truly yours,

O.W. Cobb

File: CN1-M-Western Farmers, Pt. 4

qhb,5

WESTERN FARMERS ELECTRIC COOPERATIVE
Post Office Box 429 Anadarko, Oklahoma 73005
405-247-3351

June 15, 1983

Mr. O. W. Cobb
Vice President
Coal & Taconite Pricing
Burlington Northern Railroad
176 East Fifth Street
St. Paul, Minnesota 55101

Dear Mr. Cobb:

Thank you for your letter of June 2. We are very disappointed that the Burlington Northern believes it cannot grant Western Farmers trackage rights for its own coal movement, particularly after our consultant's advice that such operation would bring us significant savings.

We have carefully studied the costs of operations over trackage rights, and the results show very substantial savings compared to coal transportation from you at rates projected under the new Ex Parte 347 as the ICC pendulum continues to swing in favor of rail carriers. We would be happy to compare our studies with any you have undertaken in concluding that we would incur "considerably greater cost" using trackage rights than under your rates.

We are not aware of any "regulatory obstacles" to your leasing trackage rights to Western Farmers. This was also a matter of considerable study before we made our request. Would you please explain why you believe you are "without power" to grant our request, and identify the regulatory obstacles you doubt could be overcome.

Unless you make known to us matters we have not taken into consideration, we would prefer to go forward as I proposed on April 4. To save time and obviate your apparent regulatory concerns, we would be willing to hold the Burlington Northern harmless for any liability it might incur in leasing trackage rights to Western Farmers. Of course, we are willing also to consider any other approach you may suggest to hold down the coal rail transportation costs which have affected our customers so much more severely than those of our competitors in Oklahoma.

Sincerely,

Marvin Scherler

Marvin Scherler
President

BURLINGTON NORTHERN RAILROAD

O.W. COBB
Vice President
Coal & Taconite Pricing

176 East Fifth Street
St. Paul, Minnesota 55101

Mr. Marvin Scherler
President
Western Farmers Electric Cooperative
P. O. Box 429
Anadarko, Oklahoma 73005

July 29, 1983

Dear Mr. Scherler:

In response to your letter of June 15, I must reaffirm my earlier advice that Burlington Northern views your trackage rights proposal as unworkable and impractical.

While we have not undertaken any hypothetical cost studies of proposed trackage rights operations, I am confident, based on our experience as a trackage rights tenant and grantor as well as our knowledge of labor requirements, that you would not achieve the cost savings you hope for. Wholly apart from the usual maintenance, operations, labor and rental costs associated with trackage rights operations (and these vary considerably), proposed operations by a tenant over major BN coal lines of some 1,350 miles in length raise major and unpredictable operational and feasibility problems. I am unaware of any functioning trackage rights arrangement of the scope you suggest where the tenant is an experienced common carrier, let alone where the proposed tenant is not a railroad.

In addition to cost and operational problems which make your proposal impractical, as I indicated previously, we believe there are regulatory obstacles which make your suggestion unworkable. Just recently--on July 20--the ICC served a decision in Ex Parte No. 347 (Sub No. 1) which held that trackage rights may be granted by the ICC only where there is an agreement between the parties and the parties are rail carriers. A copy of the decision is attached for your convenience. Western Farmers is not a common carrier and therefore could not be the recipient of trackage rights. Nor do we believe Western Farmers could reasonably expect the Commission to grant it a certificate of public convenience and necessity to conduct common carrier operations. A shipper's proposal to conduct railroad operations solely for its private benefit is, in our view, inconsistent with common carrier obligations and

the public interest under the Interstate Commerce Act. We are unaware of a single instance in which a shipper has been authorized to so act and there are numerous cases holding analogous proposals to be unlawful or improper.

Finally, as you are undoubtedly aware, some coal shippers have advocated trackage rights oprations as an alternative stand-alone cost methodoloty in Ex Parte No. 347 (Sub No. 1). We believe it would be inappropriate for us to explore your proposal while such contentions are being advanced for use in rate reasonableness proceedings, such as that pending between our two companies. While I must again decline your trackage rights proposal, I remain interested in attempting to resolve our differences and am willing to consider more realistic and accepted alternatives.

Very truly yours,

File: CN1-M-West. Farmers

gfb,2

for Mr. Mo...
from ... Kunkel
Washington, D C.

EC

REC'D. LAW DEPT.
JUL 22 1983
BN ST. PAUL
SERVICE DATE
JUL 20 1983
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INTERSTATE COMMERCE COMMISSION

DECISION

EX PARTE NO. 347 (Sub-No. 1)

COAL RATE GUIDELINES--NATIONWIDE

Decided: July 14, 1983

In the decision served February 24, 1983, we proposed a maximum rail rate policy applicable to captive coal traffic and requested comments. Under the proposed "constrained market pricing" approach, rail carrier pricing of market dominant coal traffic would be subject to four upward constraints. Under the first constraint, we proposed that a coal shipper could not be charged more than the "stand-alone cost" of serving its traffic.

We have issued a Notice of Intent to Prepare an Environmental Impact Statement and Statement of Energy Impact and Proposed Scope (served February 28, 1983) in this proceeding. In the notice, we set forth specific questions about the energy and environmental effects of setting maximum rail rates for captive coal traffic. NERCO, Inc., Potomac Electric Power Company, Public Service Company of Indiana, Inc., South Carolina Public Service Authority, and System Fuels, Inc. (petitioners) on April 28, 1983, filed joint comments on the notice and on environmental issues generally. In the same document these parties made a request for institution of a new rulemaking under 49 U.S.C. 10526 for institution of mandatory trackage rights to shippers as an alternative basis for assessing stand-alone costs. The parties' comments on the environmental issues will be dealt with in the environmental phase of this proceeding. This decision deals with the request for a further rulemaking.

In support of their request, petitioners maintain that the stand-alone cost concept, which we have defined as representing that level at which the shipper could provide the service itself,

is an unworkable theoretical fiction and, therefore, that we must consider some other method for permitting shippers to provide transportation by rail for themselves. Petitioners base their analysis on 49 U.S.C. 10701a, which requires rail rates to be reasonable; and on the theory of stand-alone costs that, according to petitioners, requires shippers to be able to "fend for themselves." Petitioners argue that requiring railroads to grant trackage rights to shippers at rental fees currently paid by one railroad to another would provide an alternative means of computing stand-alone costs that would avoid the energy and environmental problems associated with high coal shipping rates or shifts by shippers to other modes of transportation or energy products. Accordingly, petitioners request that we begin "a rulemaking proceeding for the institution of mandatory trackage rights as an alternative to stand-alone costs, should they be implemented." Request for Rulemaking at 25. The desired outcome of such a rulemaking would be a Commission finding that "a hypothetical stand-alone cost [is] unreasonably high if it exceeds the shippers' [sic] actual ability to transport its coal on the railroad by its most efficient means." Request for Rulemaking at 22-23. If the rate is found unreasonably high, the Commission would mandate trackage rights and set the associated rate.

To begin a rulemaking, it is necessary that we have a statutory basis for exercising jurisdiction over the subject matter. Section 10701a does not confer jurisdiction with respect to trackage rights; rather, that section sets standards for rail carrier rates.

The only provision of the Interstate Commerce Act granting the Commission jurisdiction over trackage rights is set forth at 49 U.S.C. 11343(a)(6), which provides that acquisition by a rail carrier of trackage rights over a railroad line owned or operated by another rail carrier may be carried out only with Commission

approval. When approval of an agreement is granted, it is merely permissive in nature (unless in the context of a condition to another transaction).

The coal shippers' proposal fails to meet the statutory criteria for exercise of Commission authority over trackage rights, namely (1) that there be an agreement between the parties, and (2) that the parties be rail carriers. Under the statute, an agreement between carriers is essential to approval and consummation. Boston & Maine Corp. Trackage Rights Over Conrail, 360 I.C.C. 239 (1979). Generally, we have no power under section 11343 to compel a railroad to grant trackage rights over its lines to another carrier [Baltimore & O. R. Co. Operation, 261 I.C.C. 535, 544 (1945); Alabama T. & N. R. Corp. Construction, 124 I.C.C. 114 (1927); and Mazner-O'Hara Scenic Railway--Operation--In the State of Michigan (not printed), served November 20, 1980], much less to a shipper. The Commission does have the power to impose trackage rights where there is no agreement, but only as a condition to a rail consolidation. Louisville and Nashville Railroad Co. v. United States, 369 F. Supp. 621 (D.C. Ky. 1973) aff'd 414 U.S. 1105 (1973). The power to condition approval does not, however, eliminate the requirement that an agreement must be reached between the parties. 360 I.C.C. at 241. Also, under the statute, the trackage rights agreement must be between or among carriers.

Since (1) the statute confers jurisdiction concerning trackage rights only when there is an agreement between two or more railroads and (2) petitioners' proposal fails to satisfy either of these requirements, we deny the request to begin a rulemaking for lack of subject matter jurisdiction. . . .

Petitioners assert that if we decline to institute a rulemaking, we must nonetheless consider forced trackage rights as one alternative under the environmental assessment. As noted

above, this issue will be dealt with in connection with the assessment itself.

Petitioners also argue that we must attempt to quantify the difference between costs established on the basis of trackage rights plus shipper acquisition of equipment and crews (a "modified" stand-alone cost theory), on the one hand, and stand-alone costs as proposed by the Commission in Ex Parte No. 347 (Sub-No. 1) on the other. This issue will be addressed in the overall decision in this case based upon comments, and, as necessary, in individual proceedings as well.1/

This action will not significantly affect the quality of the human environment or the conservation of energy resources.

It is ordered:

1. The petition is denied.

2. This decision is effective on July 21, 1983.

By the Commission, Chairman Taylor, Vice Chairman Sterrett, Commissioners Andre and Gradison.

(SEAL)

Agatha L. Mergenovich
Secretary

1/ With regard to individual adjudications, we note that the trackage rights argument in regard to stand-alone costs has been raised in No. 36114 (Sub-No. 1), Potomac Electric Power Company v. Consolidated Rail Corporation, and will be addressed there.

WESTERN FARMERS ELECTRIC COOPERATIVE
Post Office Box 429 Anadarko, Oklahoma 73005
405-247-3351

October 21, 1983

Mr. N.P. Moros
General Counsel-Commerce
Burlington Northern Railroad Company
176 E. 5th Street
St. Paul, Minnesota 55101

Dear Mr. Moros:

Since early April we have been trying to obtain a lease of trackage rights from your company to move our unit coal trains. Now, half a year later, for the first time we have been directed to contact you for a response. Having already wasted six months, we want to meet with you on this matter as soon as possible -- next week at the latest. Western Farmers' business of power supply to its member cooperatives is in jeopardy. The BN's charge for moving coal for boiler fuel over its rail line is the principal cause of the problem.

On April 4, we first wrote to your colleague, Mr. O.W. Cobb, asking Burlington Northern to lease trackage rights to Western Farmers to facilitate Western's transporting its own coal from our Wyoming mine source to our Oklahoma generating plant. Having heard nothing, after nearly two months, we asked your president, Mr. W.A. Drexel, for a response to our request. Shortly afterward, we received a letter from Mr. Cobb indicating that the BN believed it was without power to grant us trackage rights and suggesting that we would not obtain reduced transportation costs under our proposed operations, even if all regulatory obstacles, ultimately, could be overcome.

We wrote back, urging Mr. Cobb to reconsider, because our studies had projected very substantial cost savings (as much as $6 to $9 a ton) from hauling our own coal with trackage rights over the BN, and we knew of no "regulatory obstacles" to doing so. Mr. Cobb replied on July 29, 1983. He confessed that the railroad had made no studies, but still expressed confidence that we would not save anything by operating over trackage rights. He repeated that regulatory obstacles barred the way and enclosed an Interstate Commerce Commission decision which he said would prohibit the BN from leasing trackage rights to our cooperative. He declined our proposal, but offered to consider other alternatives to resolve our differences.

We accepted Mr. Cobb's offer to talk and met with him in Washington on Thursday, October 13. Among other things, we pressed for an explanation of why the BN felt it had to reject our trackage rights request. To our surprise, Mr. Cobb told us he was the wrong person to ask about trackage rights. You were the person we would have to talk to about them. Of course, he could have told us that back in April when he got our first letter, and your president, Mr. Drexel, certainly could have set things straight when we made our request to him on June 2.

I am sure you will understand our desire to make up this lost time and try and find a solution for Western Farmers. We think trackage rights is that solution.

Please tell us when you will meet with us. We can come to St. Paul if that would be best for you, or we can meet in Anadarko, Oklahoma City, Washington or some other mutually convenient place. I cannot overemphasize the gravity of Western Farmers' situation and the need to deal with it promptly.

Very truly yours,

Robert A. Orme
Acting General Manager

RAO:sw
cc: President Drexel
Mr. Cobb

BURLINGTON NORTHERN RAILROAD

LAW AND
GOVERNMENT AFFAIRS
DEPARTMENT

176 East Fifth Street
St. Paul, Minnesota 55101
Telephone (612) 298-2121

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October 26, 1983

Mr. Robert A. Orme
Acting General Manager
Western Farmers Electric Cooperative
P. O. Box 429
Anadarko, Oklahoma 73005

Dear Mr. Orme:

I was surprised to receive your letter of October 21 again expressing a desire to obtain trackage rights to operate coal trains over Burlington Northern to your generating facilities in Oklahoma. In June and July of this year Mr. Cobb wrote to you and explained why Burlington Northern could not entertain your proposal. Apparently, however, our position has not been made sufficiently clear.

Let me dispel any misunderstanding you may have. Burlington Northern's unequivocal position is that it will not entertain or discuss further your trackage rights proposal. Further correspondence from you on the subject of trackage rights would not be productive.

I trust this will finally put the matter to rest and permit our respective companies to devote their energies to more fruitful endeavors.

Very truly yours,

Nicholas P. Moros
General Counsel-
Administrative Law

NPM:rmc

cc: Messrs. W. A. Drexel
J. H. Hertog

EXHIBIT NO. 2

"Wheeling" Coal: An Antitrust Alternative To ICC Rate Making

By WALLACE E. BRAND and DAVID A. LECKIE

The following article draws parallels between the position of an electric utility requested to transmit electric power for the benefit of third-party buyers and sellers with whom the utility may be connected but who lack a direct connection themselves, and the position of a railroad which forms the sole land transportation link between a producer-seller of coal and its electric utility customer purchasing coal for use as a primary fuel in power generation. The authors suggest that the federal courts can remedy any unreasonable refusal to grant trackage rights for the transport of coal by the seller or purchaser in much the same way that they have remedied refusals to "wheel" electric power between a third-party seller and third-party purchaser.

If anything is more jealously protected than an electric utility's control over the right to wheel power over its transmission lines, it must surely be a railroad's control of access rights to its tracks, or "trackage rights." These are rights that other railroads or even shippers could use to compete with the owning railroad for service to captive customers. The "wheelage" charges for such use are the equivalent of wheeling charges for electric utilities. Like electric transmission lines, railroad tracks are frequently a "bottleneck," or "essential facility." Neither can be duplicated economically. In each case control of the facility confers the power to exclude competition that depends on its use. This power has been so important to electric utilities and railroads that both industries have fought hard and successfully to avoid significant control by their principal regulators over competitors' access to those vital facilities.[1]

Paradoxically, it was this effective immunity from regulation that proved so crucial in breaking the transmission bottleneck in the electric utility industry. It made wheeling of electric power a "voluntary commercial relationship" subject to application of the antitrust laws, as the Supreme Court held in Otter Tail Power Co. v United States.[2] The court affirmed findings that Otter Tail had monopolized or attempted to monopolize, violating § 2 of the Sherman Act, by refusing to wheel power from other sources to municipalities that had formerly been its captive customers. The Otter Tail case reaffirmed the principle that a federal district court can remedy an antitrust violation by compelling a monopolist to grant to others the use of an essential facility. In that case, the court required the utility to wheel the electric power of others to displace power it wanted to sell.[3]

Today, electric utilities are facing the railroads' trackage bottleneck, and it hurts. Since enactment of the Railroad Revitalization and Regulatory Reform Act of 1976 ("4-R Act")[4] and the Staggers Rail Act of 1980 ("Staggers Act"),[5] the price of rail transportation of coal and other bulk commodities has skyrocketed. It is not unusual to find the delivered cost of coal shipped under the new deregulated rates as much as four times the price of coal purchased at the mine, and the full cost per kilowatt-hour of new coal-fired generation (fixed charges plus fuel) is rapidly approaching the cost of generation by oil, natural gas, and even the more recently constructed nuclear generators. Many electric utilities are effectively locked into long-term coal supply contracts by decisions made in response to the Powerplant and Industrial Fuel Use Act of 1978[6] and to "bait and switch" quotations of rates much lower than those ultimately charged by the railroads. They have tried to get relief from the Interstate Commerce Commission but without much success.

In many cases, the Staggers Act renders the ICC powerless to help. Before the ICC can entertain a complaint that the rate demanded by a railroad is too high, it first has to find that the railroad has "market dominance."[7] If the railroad is not found to have market dominance over the movement, it can charge any rate it likes. Rates below a certain "revenue-variable cost percentage" are automatically exempt from regulation, and disputes over what should be included in the "revenue-variable cost percentage" may have the effect of raising the level of rates free of regulation. The ICC's encouragement of

Endnotes appear beginning on page 30.

contract rates for coal movements is likewise a problem for utilities, because those rates are effectively immune from regulation.[8] The ICC's emphasis on negotiating rates assumes that the electric utility has enough bargaining power to elicit a reasonable contract proposal.

Even if the ICC can and will entertain a utility's complaint, bringing such an action is very much akin to kicking a sponge 500 miles long. No matter how much energy or money one applies to making a case, the end result, taking into account judicial review and possible remand, is likely to be long in coming. Moreover, the ICC's record under the recent legislation suggests that concern to restore financial integrity to some of the nation's railroads has eclipsed its historic role of assuring adequate service at reasonable, nondiscriminatory rates for all shippers. The ICC's remarkable gyrations in the drawn out "market dominance" proceeding, Ex Parte No. 320, indicate the lengths to which it is prepared to go in advancing railroads' interest in subsidizing their competition in noncaptive markets at the expense of captive bulk commodities shippers like the coal-dependent electric utilities.[9] In November, 1983, the fifth circuit overturned en banc what had been a somewhat favorable panel decision on the issue of how "market dominance" is to be determined.[10] The full court dashed shippers' hopes that consideration of "geographic" and "product" competition would be excluded from the test. Even the panel had refused to establish presumptions of dominance based on market share, cost, and substantial investment, as the shippers had sought, and the en banc court adopted its decision affirming the ICC on these issues.

The rule making to provide guidelines in the pricing of coal transportation, Ex Parte No. 347, is another example. The proposed policy announced in the ICC's Ex Parte No. 347 (Sub-No. 1) decision in that proceeding, will scuttle any chance of obtaining a decent rate even where the ICC finds market dominance.[11] The decision contemplates rate increases of 15 per cent per year plus inflation on captive coal traffic until a railroad achieves "revenue adequacy." Although innocent sounding, the term "revenue adequacy" means that a railroad can charge enough to pay for all its capital at current money market costs, no matter how little its embedded cost of debt actually is. This cost of capital is applied to an original-cost *undepreciated* rate base, whether the property is one year old or fifty years old, and without regard to whether it is used and useful or unused and unuseable.[12] But the railroads still were not satisfied, and now the ICC is considering whether or not to inflate the standard even more by applying the current cost of capital to a *replacement-cost* rate base.

According to the ICC, 15 per cent annual increases, if applied to all coal traffic, likely would allow most of the nation's coal hauling railroads to achieve revenue adequacy within eight years under the proposed policy. It will surely take longer if the ICC inflates the revenue-adequacy standard as it is considering doing.

Perhaps the shippers' last hope at the ICC was the Long-Cannon Amendment. That provision of the Staggers Act, codified at 49 USC § 10707a(e)(2), was designed specifically to give added protection to captive shippers because of Congress' concern about the extent to which railroads might use their monopoly traffic to subsidize their competitive traffic. If a proposed rate increase meets a special, particularly rigorous market dominance threshold, the ICC must consider certain factors in determining whether to investigate the increase and, if it decides to investigate, in determining whether the proposed rate is reasonable. These factors focus on whether captive shippers are contributing an unreasonable share of a railroad's revenue. The ICC rejected a petition for rule making to implement the Long-Cannon Amendment and announced a policy on its implementation.[13] It said it would address the Long-Cannon factors only in individual cases and only to the extent the parties presented evidence on them. The burden on shippers, given the ICC's tight statutory deadlines for deciding whether or not to investigate (protests must be filed in ten days) and for deciding rate cases, and the fact that only the railroads will have the relevant information, is mind boggling. While questioning some provisions of the ICC's policy statement, the District of Columbia circuit declined to review it — and affirmed the ICC's decision not to institute a rule making.[14]

Faced with the gloomy prospect of rate litigation before this now unpropitious forum, electric utility coal shipp s may want to consider whether further reliance on the ICC for protection against monopoly pricing is warranted. It may pay them to look instead to the courts and the antitrust laws for help in breaking the railroads' bottleneck.

An Antitrust Alternative

The essence of a coal shipping utility's antitrust claim would be that the defendant railroad has misused its control over its tracks: an essential facility constituting the only practical means of getting coal to the utility's plant. If the railroad has refused to make the use of the tracks, or "trackage rights," available on fair terms, the utility would seek such rights as relief from the court, along with treble the damages suffered as a result of the refusal.

Since many electric utilities now own their own coal

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hopper cars or gondolas, they would need only to purchase or lease locomotives (and cabooses) and provide their own labor to have an efficient, low-cost alternative to service by a monopoly railroad. Senators Wendell H. Ford and Russell B. Long suggested this very remedy in the Senate's hearings on S 796, the administration's version of the legislation that emerged as the Staggers Act. They raised the possibility that the proposed legislation could provide the right to obtain the vital trackage rights necessary to free captive coal shippers from the railroad monopoly.[15] While the legislation enacted did not incorporate their proposal, this article suggests that those trackage rights may be available to electric utilities without legislation — through litigation under the antitrust laws.

The critical legal questions that will arise in pursuing trackage rights through the antitrust laws fall into two categories: (1) Can the electric utility get into the antitrust court, and (2) can it come back out with a useful result?

The first category includes the issues of exclusive jurisdiction and primary jurisdiction. Attempts to seek antitrust remedies against railroads will undoubtedly be met by claims that the ICC has exclusive jurisdiction over the matters complained about. Exclusive jurisdiction in the ICC would completely bar an antitrust claim. Alternatively, the railroads will claim primary ICC jurisdiction, urging a long and expensive detour through a proceeding at the ICC before reaching the antitrust claim.

The second category involves the factual and legal questions of liability and remedy. To come out of the court with a useful result, the utility must first establish the railroad's antitrust violation. If it can do so, it will then be in a position to obtain an injunction requiring the railroad to lease trackage rights on fair "wheelage" terms and to obtain treble damages and attorneys' fees.

Getting into the Antitrust Court

To overcome a railroad's claim of exclusive jurisdiction, the electric utility must show the following: (1) Neither the Interstate Commerce Act nor the antitrust laws explicitly immunize the railroad's conduct from liability and enforcement; (2) the Interstate Commerce Act is not a pervasive scheme of regulation; (3) the Interstate Commerce Act does not imply an exemption from the antitrust laws; and (4) there is no plain repugnancy between the specific relief requested of the antitrust court and the authority of the ICC to control the activities contemplated by that relief. It should be possible to make the required showings in the present circumstances.

First, the Interstate Commerce Act does not explicitly exempt rail carriers from the operation of the antitrust laws except in certain respects not relevant here.[16]

Second, ICC regulatory jurisdiction cannot be deemed pervasive, since the courts have already applied the antitrust laws to the rail industry. Compare Pan American World Airways v United States (1963) 371 US 296, which found pervasive regulation of airlines, with Georgia v Pennsylvania R. Co. (1944) 324 US 439, which applied the antitrust laws to railroads notwithstanding their regulation. If ICC regulatory jurisdiction over railroads was not pervasive before the 4-R Act and the Staggers Act, with their emphasis on deregulation, a fortiori it is not pervasive now.

Third, implied exemptions from the antitrust laws are not favored. The general rule is that an exemption will be implied only when and to the extent necessary to make a regulatory scheme work. There is no basis for an implied antitrust exemption where the ICC's regulatory scheme permits maximum railroad rate regulation only after a finding of market dominance. The regulation is intended to be only a last resort. Railroads and shippers are encouraged to make rates through the application of market forces to the extent possible. The regulatory scheme contemplates voluntary commercial arrangements, with the antitrust laws functioning as referee to make the process work. Moreover, contracts are the favored rate-making tool, and ICC review of contract rates is extremely limited, Congress having expressly stated its intent that the antitrust laws will apply to contract rate making.[17]

Nothing in the Staggers Act states or even suggests that the availability of ICC maximum rate making for rail transportation service in market dominance situations forecloses antitrust liability based on a monopoly railroad's refusal to grant trackage rights. Nor should it foreclose injunctive relief in the form of an order compelling the grant of trackage rights and damages based on the difference between the monopoly rates charged and the cost of transportation that the utility would have experienced if the rights had not been refused. On the contrary, ICC maximum rate making and market rate making subject to antitrust standards are not mutually exclusive, but rather are alternative approaches to the same result. What is more, Congress favors the market rate-making approach. As of 1980, it is expressly the policy of the United States in regulating the railroad industry "to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail."[18] To the same effect, the Staggers Act Conference Report states the conferees' belief that, "by allowing the forces of the marketplace to regulate railroad rates *wherever possible* the financial health of the railroad industry will be improved and will benefit all parts of the economy, including shippers, consumers, and rail employees."[19]

David A. Leckie is a member of the law firm of Brand & Leckie, where he specializes in litigation applying antitrust law and policy to regulated industries. He was formerly (1979-81) deputy general counsel and chief trial counsel of the Federal Energy Regulatory Commission and, before that (1972-77), a trial attorney and assistant section chief in the antitrust division of the Department of Justice. **Mr. Leckie** received a JD degree from the University of Oregon and a BA degree in political science from the University of California at Berkeley.

Fourth, there is no plain repugnancy between the ICC and antitrust statutory schemes regarding the compelling of trackage rights. Under these circumstances the court will enforce both statutory schemes.[20] The ICC has only limited jurisdiction in this area. It can require trackage rights to provide access to terminals,[21] to make shipper-owned short lines viable,[22] and to condition mergers or joint activity.[23] It has jurisdiction to approve voluntary trackage rights agreements between rail carriers,[24] but has proposed to exempt those from regulation.[25]

The ICC recently held that it cannot compel trackage rights agreements between railroads except in the limited circumstances just mentioned and — most important — that it lacks power and authority altogether over railroad grants of trackage rights to coal shippers. This question arose in connection with the Ex Parte No. 347 proceeding to determine appropriate rate-making principles for coal transportation. A participant in the proceeding urged the ICC to adopt a rule mandating trackage rights to coal shippers as an alternative basis for assessing stand-alone costs under the commission's contemplated methodology. The proposal suggested that trackage rights at rental fees currently paid by one railroad to another would be appropriate. The ICC rejected the idea.

Searching for a necessary "statutory basis for exercising jurisdiction over the subject matter," the ICC fixed on 49 USC § 11343(a)(6) — "the only provision of the Interstate Commerce Act," according to it, "granting the commission jurisdiction over trackage rights." But that provision did not suffice: It required an agreement between the parties, and the parties had to be rail carriers. The ICC concluded that it had "no power under § 11343 to compel a railroad to grant trackage rights over its lines to another carrier [citations omitted] *much less to a shipper.*"[26] As with railroad rate making, trackage rights grants to both railroads and shippers involve voluntary commercial relationships subject to the antitrust laws.

The proviso of § 16 of the Clayton Act,[27] which forbids private suits for injunctions "against any common carrier subject to the provisions of [the Interstate Commerce Act] in respect of any matter subject to the regulation, supervision, or other jurisdiction of the Interstate Commerce Commission," has been construed essentially to forbid private suits for injunctive relief where the ICC has exclusive jurisdiction of the matter in controversy. It was held not to bar the state of Georgia's suit challenging a railroad rate-fixing conspiracy.[28] The ICC had jurisdiction to determine ultimately the railroads' lawful rates. But according to the Supreme Court, it did not have jurisdiction over a conspiracy by which the railroads got together and decided what rates they would file. An injunction to remove the influence of such an unlawful conspiracy from the rate-making process was therefore not foreclosed by the § 16 proviso.

A particularly illustrative and helpful case on this point is Seatrain Lines v Pennsylvania R. Co.[29] Seatrain, a water carrier, complained of certain railroads' refusal to interchange freight cars with it as they did freely with one another. The ICC had duly approved the railroads' car interchange agreement. It had also ruled that it had no control or authority over the railroads' withholding of cars from water carriers with which the railroads did not share through routes, and it had, therefore, refused to require the railroads to modify and expand their agreements as Seatrain wanted. The third circuit likewise refused to declare the railroads' agreements unlawful or to require their expansion. It cited the § 16 proviso and the ICC's plenary power to regulate and control interchange of freight cars among railroad companies. However, because the ICC had "plainly ruled that it has no control or authority over" the railroads' withholding of cars from Seatrain, the court found no bar to Seatrain's antitrust suit against the railroads' conspiracy to deny Seatrain freight cars. According to the court:

> It follows that whatever relief, whether by injunction or the award of damages, may be appropriate under the antitrust laws in connection with this aspect of the alleged conspiracy can be granted without encroachment upon any area of commission concern or violation of the prohibition of § 16 of the Clayton Act against enjoining activity within the regulatory power of the commission.[30]

The resemblance of the ICC's denial of power and authority over trackage rights to coal shippers to the situation in Seatrain is striking, and the conclusion that § 16 would not bar a coal shipper's suit for refusal to grant trackage rights seems inescapable.

Two very recent cases reinforce the conclusion that the ICC does not have exclusive jurisdiction in this area. Motions to dismiss on that ground were rejected in Transkentucky Transportation Railroad v Louisville & Nashville Railroad Co.[31] and Pinney Dock & Transport Co. v Penn Central Corp.[32]

Transkentucky involved an attempt by a project combining a short rail line, coal transport facilities, and use of inland waterways to compete with coal-hauling railroads in the eastern United States. The railroads allegedly refused to set rates for some shippers attempting to reach the project, established rates designed to discriminate against the project and exclude it from the marketplace, refused to provide access across their property and instituted sham regulatory proceedings. They tried to characterize Transkentucky's antitrust suit as an attack on the level of their rates and, therefore, subject to the exclusive jurisdiction of the ICC. The district court noted first the compatibility of Interstate Commerce Act and antitrust law objectives, particularly after enactment of the Staggers Act. It found no regulatory mandate or approval for any of the challenged conduct. Moreover, it viewed the case not as a challenge to the railroads' rate level but as dealing with a broad pattern of conduct designed to destroy a competitor, with damages measured by business losses, not by the difference between existing rates and some hypothetical rate. The complaint simply did not put in issue the lawfulness of the defendants' rates. The district court rejected the defendants' proposition that § 16 barred injunctive relief touching

on any matter subject to ICC regulation, citing Georgia v Pennsylvania R. Co.

In Pinney Dock, the district court held that the defendant railroads' only antitrust exemption for collective rate-making activities was the express immunity conferred by 49 USC § 5(b) (now 49 USC § 10706); they had no implied antitrust immunity based on pervasive rate regulation by the ICC. The railroads therefore had no protection from an antitrust suit for an alleged conspiracy involving misuse of the rate bureau system to eliminate a competitor and monopolize the iron ore dock services business. The conspiratorial activities alleged included refusing to grant a competitive rail rate for ore carriage from the plaintiff's dock, placing the dock in a switching district where it was ineligible for competitive rail rates, and imposing unjustifiably high switching charges on the cars of a rail competitor that sought to carry ore from the dock. Notwithstanding the admitted involvement of rate bureau rate-making processes in the scheme, the district court held that the conspiracy fell "outside the bounds of day-to-day railroad rate making" and was therefore fully subject to antitrust sanction.[33]

While a finding of primary jurisdiction would not bar an antitrust claim, it would likely lead to a time consuming and expensive detour through the agency that would certainly reduce the efficacy of antitrust litigation to obtain relief. The defendant railroad would argue that the antitrust court must let the ICC proceed first because the agency's views on matters within its special competence may be necessary or helpful for the court's resolution of the antitrust case. The electric utility plaintiff has a good response. The two alternatives for rate making (ICC regulation and operation of market forces) suggest concurrent jurisdiction in the ICC and the antitrust court, not primary ICC jurisdiction. The ICC would have nothing to contribute to the court's trial of the antitrust case. While it could find the presence or absence of railroad "market dominance," that would not be conclusive of the more elaborate monopoly power finding that an antitrust court must make. Nor could the ICC assist the court with the question whether a railroad's refusal to grant trackage rights to an electric utility shipper is unreasonable because, as already noted, it has no jurisdiction to compel or approve such trackage rights.

In fact, the ICC told one complainant, Mobil Oil Corporation, which sought access to alternative rail carrier service over the tracks of the Burlington Northern, to take its case to the antitrust courts.[34] Accordingly, there would be no sound reason for the court to refer the case to the ICC. The Otter Tail court did not require preliminary resort to the Federal Power Commission even when that commission urged that it should. Similarly, the tenth circuit reversed a district court in Kansas which wanted to send Sunflower Electric Cooperative's antitrust complaint to the FPC on primary jurisdiction grounds.[35] Also, in Sunoco Energy Development Co. v Burlington Northern, Inc.,[36] the Wyoming federal district court held that the ICC had neither exclusive nor primary jurisdiction over the market allocation agreement complained of, where the ICC had long had a copy of the agreement but had not approved it and had never been asked to do so.[37]

Getting Out of the Court with a Useful Result

An electric utility will leave the antitrust court with a useful result if it can (1) establish antitrust liability, (2) obtain an injunction compelling the railroad to grant trackage rights from the mine to the generating plant at a reasonable cost, and (3) obtain an award of treble damages and attorneys' fees.

Liability

As in Otter Tail, an electric utility plaintiff would plead monopolization in violation of § 2 of the Sherman Act. The monopolization offense consists of (1) the possession of monopoly power — the power to control prices or to exclude competition — in a relevant market and (2) the willful acquisition or maintenance of that power.[38]

To make out its case, the utility first would have to show that the defendant railroad has monopoly power in one or more relevant markets involving its coal transportation activities.

Definition of the relevant market or markets involves establishing what service or services could feasibly meet the utility's needs and the geographic area within which the utility could realistically seek out sellers of the relevant service. The most obvious service market is the transportation of large quantities of coal for electric utility generation. It will probably be possible also to establish a market for trackage rights since these are a "factor of production" necessary to provide the service of transportation of coal. The classic example of such a factor market is Judge Learned Hand's definition of a relevant market for "virgin" aluminum ingot in the Alcoa case.[39] Closer to home for electric utilities, antitrust review proceedings at the Nuclear Regulatory Commission have found relevant markets for "power exchange services," including wheeling and other factors used by electric utilities to produce their bulk firm power supply.[40]

The defendant railroad can be counted upon to claim that other fuels, such as natural gas, and other modes of transportation, such as barge and coal slurry pipelines, should be included in defining a broader "fuel transportation" market and that trackage rights are not a market because there is no trade in them, and certainly not between railroads and shippers.

The facts that induced the electric utility to choose coal as its generating fuel, to contract for its coal supply with a specific mine, and to site its generating plant will ordinarily answer the first claim. Although the defendant railroad would try to make the market broad enough that it could not be found to have monopoly power over it, the existence of long-term coal supply contracts, the infeasibility of truck, barge, or slurry pipeline service and of substituting gas in facilities built to burn coal, as well as the higher cost of gas or other alternative fuel, would be probative of a market limited to rail transportation of coal. As for trackage rights, railroads deal in

them extensively among themselves. Agreements for such rights cover about 8 per cent of main line track nationwide, according to the Department of Transportation.[41] Moreover, trackage rights assignments to shippers are not unprecedented.[42]

The electric utility's preferred geographic market for rail transportation of coal will usually be the point-to-point movement from mine to plant (including the trackage of other rail carriers, if any, that might be used under cooperative arrangements with the defendant railroad). The geographic market in trackage rights will ordinarily be coextensive with the bottleneck line, since the cost of duplicating that line, probably $1 million per mile or more, would be prohibitive. As with the service markets, the defendant railroad will try to expand the scope of the geographic markets. The key to defining the markets in the most useful manner will be for the plaintiff utility to show, first, that there is no other way to get its coal supply from the mine where it is produced to the plant where it is to be used and, second, that any transportation alternatives available before the plant was sited and the coal supply contracted for have been overtaken by those events.

The ICC has adopted terms coined by the Department of Justice to describe these relevant markets. The term "ex ante" refers to the coal supply choices available to the electric utility before it has contracted for its long-term supply of coal from a specific mine and before it has selected a specific site for its generating unit. After these decisions have been made, the utility is locked into an "ex post" market and most of the transportation alternatives in the ex ante market are no longer of any value. See Union Pacific — Control — Missouri Pacific; Western Pacific (1982) 366 ICC 459, 535.

If the utility succeeds in defining the relevant markets as ex post, the defendant railroad probably will have a 100 per cent share of both the coal transportation market and the trackage rights market. This is ordinarily more than sufficient for the necessary finding of monopoly power.[43] In addition, however, it should be evident in most cases that the railroad actually can control the price of coal transportation service over the point-to-point route between the coal mine and generating plant and it can exclude competition from that route. It also will have the exclusive power to determine whether any party other than itself will be able to run coal unit trains over that route and probably the exclusive right to set the price for any rights to do so that it may grant. To put it another way, the railroad's tracks will constitute an "essential facility" — because it controls them, the electric utility would be unable practically or reasonably to duplicate them, and as will be discussed, it would be feasible to permit their use under a trackage rights lease. See, MCI Communications Corp. v American Teleph. & Teleg. Co. (CA7th 1983) 708 F2d 1081, 1132, 1133, certiorari denied (1983) 104 S Ct 234.

These conclusions will be correct unless ICC regulation of rates or of trackage rights eliminates the railroad's monopoly power or the ability to exercise it. As suggested by the discussion of exclusive jurisdiction, the present regulatory scheme does not have that effect.

While the ability of other railroads to use the defendant's tracks might vitiate its monopoly power, the ICC cannot require a railroad to grant trackage rights to other railroads except in certain very limited circumstances. As noted above, the commission recently expressly held that it lacks such authority and invited a complaining seller of coal to electric utilities to seek relief in the antitrust courts. The ICC's regulatory authority likewise does not preclude the railroad's exercise of monopoly power over coal transportation, because the railroad can use its power to grant or deny trackage rights to retain its monopoly control of that market. The fact that the ICC has "last resort" jurisdiction to provide some rate remedy in the downstream coal transportation market does not preclude the exercise of monopoly power in the upstream trackage rights market, just as FPC regulation did not do so in Otter Tail or the Nuclear Regulatory Commission antitrust review cases noted above, where the argument was made and rejected even though the FPC had exclusive control over wholesale rates.

The final element of willful acquisition or maintenance of monopoly power is usually inferred from conduct which has the consequence of destroying or excluding competition. While a general intent to engage in practices which maintain monopoly power ordinarily is sufficient in monopolization cases, it should be possible (and may be necessary) to go further and prove specific intent to foreclose competition in this kind of situation. In any event, the unreasonable refusal to deal with a competitor is frequently relied upon to establish a monopolist's wrongful intent — and this is especially so where the refusal to deal involves access to an essential facility. See, MCI Communications v American Teleph. & Teleg. Co. 708 F2d 1081, at 1132, 1133. The plaintiff electric utility would therefore try to show that the railroad's refusal to lease it trackage rights was unreasonable.

The railroad probably would try to justify a refusal of trackage rights on the grounds that it has no obligation to grant trackage rights and no interest in eroding its market by doing so. It might also claim safety problems. Otter Tail made the market erosion argument, and it lost. The result here should be the same. Because the ICC lacks any authority whatsoever over railroad grants of trackage rights to shippers, the decision to grant or deny such rights appears to be left to the voluntary business judgement of the railroads, subject to review under antitrust law standards. As to safety, a fair analogy is Amtrak's trackage rights arrangement with the railroads for passenger service, even recognizing that the arrangement is in some part the product of federal statute.[44] The Amtrak experience indicates the feasibility of trackage rights grants for long hauls without foregoing safe operations (which is more important for passenger service than for freight). It suggests also that the railroads have had no problem giving up a part of what is normally considered transportation service when the market is, like passenger service, a less profitable and, hence, less desirable one than coal hauling. In the Sen-

ate hearings on the Staggers Act referred to earlier, Secretary of Transportation Adams did not testify that the mandatory granting of trackage rights for captive shippers was physically or economically infeasible but stated that it was not in the administration bill because it was politically infeasible — it simply would not pass.[46] In short, a case can be made that granting trackage rights to an electric utility for coal transportation is entirely feasible[46] and that refusing to do so is unreasonable for a monopoly railroad.[47]

There may be other good evidence available to electric utilities of railroads' monopolistic intent, in addition to unreasonable refusals to provide trackage rights. Very strong evidence might be found in railroad opposition to construction of coal slurry pipelines that could provide competitive alternatives to rail service. If, for example, two or more railroads were to agree systematically to deny rights of way across their lines to a coal slurry pipeline, that agreement would be unlawful under § 1 of the Sherman Act, as well as evidence of monopolistic intent for a § 2 case.

The same would be true of a horizontal territorial agreement to divide the market for coal transportation. Such a claim was made by Sunoco Energy Development in a federal district court in Wyoming, alleging that two railroads had contracted to divide up the shipment of coal from the Powder River basin and assigned all the mines north of Coal Creek Junction to one of them. After the district court rejected motions to dismiss based on claims of exclusive and primary jurisdiction in the ICC,[48] the defendant railroads settled the case. Another coal producer in the area then claimed that the settlement reinforced the territorial division as to other mines north of Coal Creek Junction.[49]

Injunctive Relief

As relief from a railroad's monopolization, the plaintiff electric utility would ask the antitrust court to order the railroad to offer a lease of trackage rights on fair terms, which would be the railroad's cost plus a reasonable return. The offer of trackage rights as a remedy would be consistent with the obligation to wheel imposed judicially on Otter Tail Power Company. It would not trench on the ICC's jurisdiction, for all the reasons discussed earlier. The price and terms for the trackage rights would not be subject to ICC rate regulation because the arrangement would not constitute the provision of transportation service. The arrangement would not be a "voluntary arrangement" between railroads subject to ICC jurisdiction under 49 USC § 11343. Nor would it come under other ICC authority over trackage rights. The proviso of § 16 of the Clayton Act thus would not bar such an injunction in a private case.

Where the ICC has authority to set rates for trackage rights, it has usually left it to the parties involved to agree voluntarily on such rates. After granting trackage rights in the recent Union Pacific – Missouri Pacific; Western Pacific merger case, the ICC set forth principles it would use in setting the rates for those rights absent agreement of the railroad parties.[50] The ICC's intent in that case was to preserve the competition of the railroads obtaining the trackage rights. The commission's guidelines therefore should assist the court in establishing a rate for the trackage rights it may order as injunctive relief to permit the utility to compete with the railroad. Alternatively, the court could appoint a qualified special master for that purpose.

In other instances when the ICC sets a rate for trackage rights, it is required to use condemnation principles,[51] and those can be applied by a court as easily as by the ICC and perhaps even better. One line of cases involving costs of warehousing owned by the railroads holds that contracts by railroads on terms which are so low as not to cover costs fully are subject to ICC review to the extent that they would in effect be unlawful rebates.[52] However, a rate set by the court under condemnation principles is hardly likely to invoke that jurisdiction, because the ICC uses the same principle in setting "wheelage" charges for some grants of trackage rights. Further, the changes effected by the Staggers Act may justify a different result from that in the warehousing cases.

Damages

An antitrust court could award damages even if the ICC has found "market dominance" and set a rate for the railroad's coal transportation. Such damages would be measured by the difference between an electric utility's cost of transporting its coal using trackage rights on fair terms and the price it paid under an ICC-set rate. This legal conclusion results in part because the ICC-set rate would be only a maximum rate and not one intended to foreclose lower competitive rates set by the interaction of supply and demand. In a recent proceeding, the ICC held that such competitive rates would undoubtedly be lower than the maximum rates it set for deliveries of Powder River basin coal by Burlington Northern, Inc.[53]

The railroad would undoubtedly claim that two Supreme Court cases, Keogh v Chicago & Northwestern R. Co.,[54] and Montana-Dakota Utilities Co. v Northwestern Public Service Co.,[55] preclude the utility from obtaining antitrust damages. However, both Keogh and Montana-Dakota are distinguishable from cases brought after 1980. First, both cases involved maximum *and* minimum rates (set by the ICC in Keogh and the FPC in Montana-Dakota). The ICC now has the power to set maximum rates for coal transport (which are not also minimum rates)[56] after a finding of market dominance, and, as the ICC itself has said, such rates would not be inconsistent with lower competitive rates. Second, it is no longer the intent of Congress that the ICC-set rate be the exclusive rate; instead Congress favors rates set by the market.[57] Third, damages sought would not serve to reduce an ICC-set lawful transportation rate (which Keogh and Georgia held would be impermissible) but would put the plaintiff electric utility where it would have been if the railroad had not refused it trackage rights. The district court in Transkentucky recognized the distinction: the damages legitimately sought would be measured by the plaintiff's business losses, not by the difference between an existing rate and hypothetical one.

It is likely that a railroad's costs of owning, operating, and maintaining its tracks, and of providing the necessary signaling and dispatching coordination services, are less than 25 per cent of its total costs of providing coal transportation service. Being able to provide its own transportation service with trackage rights will free the electric utility of the disadvantage of the averaging of unit train costs with the costs of all the other services provided by the railroad. Under these circumstances, the utility is likely to leave the antitrust court with a useful result.

Postscript

Electric utilities with antitrust remedies against their coal transporters must consider one important final point: regulators may cut their rates if they do not pursue those remedies vigorously. The Federal Energy Regulatory Commission set the precedent in Public Service Company of New Hampshire,[56] when it penalized that electric utility for failing to assert its contractual rights to lower-priced coal.

The electric utility had a contract to supply all coal requirements at its Merrimack plant, with deliveries scheduled to meet current requirements and maintain a 45-day stockpile. Notwithstanding the contract, the coal supplier had limited its deliveries to two unit trains each six-day period and the stockpile fell far below the 45-day minimum. The supplier had also resorted to the contract's force majeure provision to cancel many of its deliveries, and it never made up the canceled deliveries, even though the contract required makeup when the stockpile fell below the minimum level. The utility never challenged nor sought to verify the supplier's contract interpretations or its explanations for underdeliveries, even though it had reason to do so. Instead, it purchased higher-priced coal on the spot market and passed the higher costs on to its customers. The FERC found that the utility had not acted prudently in its coal procurement and had not justified including the extra cost of spot coal purchases in its fuel adjustment charge. It ordered refunds to the wholesale customers. There was no retroactive rate-making problem in correcting fuel charges found to have been improperly computed.

While the failure to enforce contract rights penalized in Public Service Company of New Hampshire might be distinguishable from a failure to assert antitrust claims against a monopolizing coal supplier, utilities who sit on such claims may be taking a serious risk that their regulators, reacting as they must to consumer pressure to keep rates down, will not make the distinction.

AUTHORS' NOTE: The authors wish to thank C. Jack Pearce, an attorney in Washington, D. C., and Sean T. Beeny, of the firm of Brand and Leckie, for their assistance in the preparation of this article.

Endnotes

[1]These regulators are the Federal Energy Regulatory Commission and the Interstate Commerce Commission, respectively. Both lack authority to compel such access except in limited circumstances. In 1978, the FERC obtained some authority to compel wheeling in § 203 of the Public Utility Regulatory Policies Act, 16 USC § 824j. The statute itself substantially limits that authority, and the FERC has read it very narrowly, most notably regarding its use to remedy anticompetitive conduct. Southeastern Power Administration v Kentucky Utilities Co. (1983) 25 FERC ¶ 61,204. The ICC's trackage rights authority is discussed later in this article.

[2](1973) 410 US 366, 97 PURSd 209.

[3]For an explication of the essential facility doctrine, see Hecht v Pro-Football, Inc. (CA DC 1977) 570 F2d 982, 992; MCI Communications Corp. v American Teleph. & Teleg. Co. (CA7th 1983) 708 F2d 1081, 1132, 1133, certiorari denied (1983) 104 S Ct 234; United States v American Teleph. & Teleg. Co. (DC DC 1981) 524 F Supp 1336, 1352, 1353, 1360, 1361. Now that the government has applied this doctrine successfully to electric utilities and telecommunications, the time may be ripe for an essential facility case in the railroad industry.

[4]PL 94-210, 90 Stat 31, codified as amended in the Interstate Commerce Act, 49 USC § 10101.

[5]PL 96-448, 94 Stat 1895, codified at 49 USC § 10101.

[6]42 USC § 8301.

[7]49 USC §§ 10701a and 10709.

[8]49 USC § 10713.

[9]See Ex Parte No. 320, Special Procedures for Making Findings of Market Dominance as Required by the Railroad Revitalization and Regulatory Reform Act of 1976, 355 ICC 874, modified (1976) 355 ICC 12, affirmed in part, remanded in part, Atchinson, Topeka & Santa Fe R. Co. v Interstate Commerce Commission (CA DC 1978) 580 F2d 625, on remand (1979) 359 ICC 735; Ex Parte No. 320 (Sub-No. 1), Rail Market Dominance and Related Considerations, 45 *Federal Register* 3355 (January 17, 1980); Ex Parte No. 320 (Sub-No. 2), Market Dominance Determinations and Consideration of Product Competition (1981) 365 ICC 118, affirmed Western Coal Traffic League v United States (CA5th 1983) 719 F2d 772.

[10]Western Coal Traffic League v United States, 719 F2d 772, adopting in part and overturning in part Western Coal Traffic League v United States (1982) 694 F2d 378.

[11]Ex Parte No. 347 (Sub-No. 1), Coal Rate Guidelines — Nationwide, decision, February 8, 1985.

[12]Ex Parte No. 393, Standards for Railroad Revenue Adequacy (1981) 364 ICC 803, affirmed sub nom., Bessemer & Lake Erie R. Co. v Interstate Commerce Commission (1982) 691 F2d 1104.

[13]Arkansas Power and Light Company, Petition to Institute Rulemaking Proceeding — Implementation of Long-Cannon Amendment to the Staggers Rail Act (1982) 365 ICC 985.

[14]Arkansas Power & Light Co. v Interstate Commerce Commission (CA DC 1984) No. 82-2219.

[15]See Railroad Deregulation Act of 1979: Hearings on S 796 before the Subcommittee on Surface Transportation of the Senate Committee on Commerce, Science, and Transportation, 96th Congress, first session, pp. 83, 84, 262, 280, 343, 345, 436, 630, and 1292 (1979). (Hereinafter "Hearings on S 796.") The assistant general manager of the Nebraska Public Power District also urged this remedy.

[16]It exempts railroads for activities or transactions contemplated by ICC-approved agreements between them. See 49 USC §§ 10706 (some rate agreements) and 11341 (pooling, consolidation or merger, acquisition of control).

[17]HR Conference Report No. 1430, 96th Congress, second session, 101, reprinted in 1980 *U. S. Code — Congressional and Administrative News* 4110, 4133. (Hereinafter "Conference Report.")

[18]49 USC § 10101a.

[19]Conference Report supra Footnote 17, at 89, 1980 *U. S. Code — Congressional and Administrative News* at 412. (Emphasis added.)

[20]United States v Trans-Missouri Freight Assn. (1897) 166 US 290, 315.

[21]49 USC § 11103(a).

[22]49 USC § 10910.

[23]49 USC § 11344(c).

[24]49 USC § 11345.

[25]Ex Parte No. 282 (Sub-No. 9), Notice of Proposed Rule Making, 47 *Federal Register* 40,668 (September 14, 1982).

[26]Ex Parte No. 347 (Sub-No. 1), Coal Rate Guidelines — Nationwide, July 14, 1985. (Emphasis added.)

[27]15 USC § 26.

[28]Georgia v Pennsylvania R. Co. (1945) 324 US 439.

[29](CA3d 1953) 207 F2d 255, certiorari denied (1953) 345 US 916.

[29]207 F2d at 261.

[30]1983-2 Trade Cas. (CCH) ¶ 65,476 (Ky 1983).

[31]1983-2 Trade Cas. (CCH) ¶ 65,607 (Ohio 1983).

[32]Also relevant is the District of Columbia circuit's recent decision finding no Interstate Commerce Act immunity for the railroads from the government's criminal antitrust prosecution on the same facts as Pinney Dock. United States v Bessemer & Lake Erie R. Co. (CA DC 1983) 717 F2d 595.

[33]Chicago and North Western Transportation Company construction and operation of a line of railroad in Niobrara and Goshen counties, Wyoming, and in Sioux and Scotts Bluff counties, Nebraska (1981) 363 ICC 906, 922-924. (Hereinafter "Chicago & N. W. Trans. Co.")

[34]Sunflower Elec. Coop., Inc. v Kansas Power & Light Co. (CA10th 1979) 605 F2d 791.

[35](D Wyo 1980) 483 F Supp 119. (Hereinafter "Sunedco.")

[36]483 F Supp 119 at 123-127.

[37]United States v Grinnell Corp. (1966) 384 US 563, 570, 571.

[38]United States v Aluminum Co. of America (CA2d 1945) 148 F2d 416.

[39]Consumers Power Co. (1977) 6 NRC 892; Alabama Power Co. (1977) 5 NRC 804, modified (1981) 13 NRC 1027, affirmed, Alabama Power Co. v Nuclear Regulatory Commission (CA11th 1982) 692 F2d 1362, certiorari denied (1983) 104 S Ct 72.

[40]Railroad Deregulation Act of 1979: Hearings on HR 4570 before the Subcommittee on Transportation and Commerce of the House Committee on Interstate and Foreign Commerce, 96th Congress, first session, 1038 (1979) (appendix to testimony of Robert E. Gallamore, deputy administrator, Federal Railroad Administration). The percentage of track subject to trackage rights agreements is much higher when branch lines and terminals are included also.

[41]See; e.g., Brotherhood of Locomotive Firemen and Enginemen v Interstate Commerce Commission (CA7th 1945) 147 F2d 312.

[42]See United States v Grinnell Corp. 384 US 563, 571 (monopoly power inferred from predominant share of market).

[43]45 USC § 562.

[44]Hearings on S 796, supra at 84.

[45]In the present Congress, bills have been introduced which effectively would declare a monopoly railroad's refusal to grant such rights to other railroads or to shippers per se unreasonable. S 2417, 98th Congress, second session (1984) (introduced by Senator Dennis DeConcini); HR 4559, 98th Congress, first session (1983) (introduced by Representative John F. Seiberling). This proposed legislation presumes implicitly that electric utility rail operation using trackage rights would be feasible and consistent with normal railroad business activity.

[46]The case would be enhanced if the defendant railroad transports Powder River basin coal. One intent of the Staggers Act, according to Congress, was to "promote needed competition for transportation of the low-sulfur coal from the Powder River basin that is used by a great number of utilities in many states." Conference Report, supra Footnote 14, at 150, 1980 *U. S. Code — Congressional and Administrative News* at 4171.

[47]Sunedco, supra Footnote 36.

[48]See Chicago & N. W. Trans. Co., supra Footnote 34, 363 ICC at 927.

[49]366 ICC at 580.

[50]49 USC § 11103(a); Missouri K-T R. Co. v Kansas City Term. R. Co. (1933) 198 ICC 4.

[51]See Baltimore & Ohio R. Co. v United States (1939) 305 US 507.

[52]Chicago & N. W. Trans. Co., supra Footnote 34, 363 ICC at 927.

[53](1922) 260 US 56.

[54](1951) 341 US 246.

[55]Minimum rates can be established under 49 USC § 10701a(c)(1), but the circumstances under which they may be so established are not pertinent here.

[56]See 49 USC § 10101a(1).

[57]6 FERC ¶ 61,299 (1979).

EXHIBIT NO. 3

Western Farmers' Correspondence With Shell Oil Company
Concerning Anticipated Excuse from Coal Contract Performance
Because of Inability to Obtain Rail Transportation
at Reasonable Cost

WFEC
WESTERN FARMERS ELECTRIC COOPERATIVE
P.O. BOX [illegible] ANADARKO, OKLAHOMA 73005 • (405) 247-3351

July 13, 1984

BY CERTIFIED MAIL

Shell Mining Company
P. O. Box 2906
Houston, Texas 77252

Attention: Marketing Department

Gentlemen:

This is to advise you pursuant to articles 8.1 and 8.4 of our contract dated October 14, 1977, as amended by agreement dated as of October 31, 1982, that we anticipate we will be prevented from performance under said contract after September 1, 1984, as a result of inability to obtain essential transportation at reasonable cost. This letter is intended to comply with the notice provision of article 12 of our contract; we are also sending a copy to Shell's assignee, Triton Coal Company.

You have been kept current on our attempts to overcome this problem. Because of our continued lack of success, Western's management now has reluctantly concluded that it will not be able to continue performance after the date indicated.

We would be available to meet with you to discuss this matter in further detail if you desire.

Very truly yours,

Thomas W. Stevenson

Thomas W. Stevenson
General Manager

cc: (By Certified Mail)
Triton Coal Company
Shell Woodcreek
P. O. Box 2906
Houston, Texas 77252

Shell Mining Company
P.O. Box 2906
Houston, TX 77252

SUBSIDIARY COMPANIES
R&F COAL COMPANY
TRITON COAL COMPANY
TURRIS COAL COMPANY

July 20, 1984

Certified Mail

Western Farmers Electric Cooperative
P. O. Box 429
Anadarko, OK 73005

Attn: Mr. Thomas W. Stevenson
General Manager

Gentlemen:

Pursuant to our service agreement with Triton Coal Company, and confirming our recent telephone conversations, we hereby acknowledge receipt of your letter of July 13, 1984, in which you advised that you anticipate that Western Farmers will be prevented from performing under our coal sales contract after September 1, 1984.

We are shocked and dismayed that Western Farmers has taken this position, and we are frankly at a loss to understand how such a decision could be reached, particularly in light of your June 29 letter which nominated 1.6 million tons for 1985. None of the information you have provided us supports your force majeure claim, and we firmly believe that your notice of termination based on this claim has no legal foundation. Any determination of force majeure under article 8.1 of the contract cannot be made by reading a single phrase, but must be interpreted in the context of the entire contract, and with an understanding of the Uniform Commercial Code and commercial contract law as it applies in determining contractual obligations.

As you know, the Western Farmers contract represented the original justification for our investment in the Buckskin Mine, and we are very disappointed that your decision could be made without reviewing the matter with us, and with no apparent consideration for the impact on the mine and its employees. We hope you will reconsider your position after a more thorough review of the law and the facts. Western Farmers has been performing under the contract, and we are not aware of any event which would affect Western Farmers' ability to perform beginning on September 1. In the absence of any evidence which supports your excuse of performance, we reject your claim and are prepared to take whatever actions may be necessary to pursue our rights and protect our employees.

The relationship we have had with Western Farmers in the past has been important to us, and your reconsideration of the position you have taken will be essential in reestablishing a mutually beneficial business relationship. We look forward to your earliest response.

Sincerely,

K. G. Cloninger
Manager Marketing

cc: J. P. Duvall
President, Board of Trustees

F. K. Blackard
President
Triton Coal Company
P. O. Box 3027
Gillette, WY 82716

Telecopi to: T. Stevenson
rom: W. Brand
July 27, 1984

July 27, 1984

Mr. K. G. Cloninger
Shell Oil Company
Two Shell Plaza
P.O. Box 2099
Houston, Texas 77001

Dear Mr. Cloninger:

This is in response to your letter addressed to me but delivered only to Mr. Duvall. It was received by him on July 26, 1984, on our return from Washington, D.C., where we had invited you to meet with us regarding the subject of this letter.

First, it is a mistake to characterize our letter of July 13, 1984, as a "notice of termination." As we understand the contract, neither party has the right to terminate except upon 90 days' notice following six months of excused non-performance. If we are able to obtain transportation at a reasonable cost we will of course continue to receive coal from you at the Buckskin mine under the contract.

Second, we do not read Section 8.1 of the contract to excuse non-performance only in the event of force majeure. It expressly provides for excuse of performance when one of the parties is prevented from performing by inability to obtain essential transportation at a reasonable cost -- which, as you know, is exactly our situation.

As you also know, we have labored under unreasonable transportation costs for several years. The 1977 price quote from the Frisco and the Burlington Northern on which we relied in executing our contract with you was $11.94/ton. Now we are paying approximately twice that. Until now we have tried to make a go of it by attempting to eliminate or ameliorate this situation. In fact we have made at least six separate efforts -- at considerable cost -- to obtain some relief. You have been aware of some of these efforts. We have solicited your assistance in some of them. We will be glad to tell you of any of which you are not aware in whatever detail you may request.

The time has come when we can no longer shoulder the burden of the Burlington Northern's monopoly rates. We are squeezed dry. Even the present costs are tearing our cooperative apart. Under the ICC's Ex Parte 347 rule the BN can double and perhaps redouble its present charges.

We recognize that the Burlington Northern's monopoly charges and our excused non-performance under the contract may well impose a hardship on Shell or Triton. We have a great deal of sympathy for any miners who may be affected. We hope you will

also sympathize with our low income rural ratepayers who are being driven to despair by our high fuel adjustment charges that they must pay as the inevitable result of the unreasonable charges of the BN. I wish you could sit with me in our Board meetings in which the end result of the BN's monopoly is brought home to us in painful detail.

We have offered to meet with you to discuss this matter fully but have encountered only your threats and your insistence on dealing with others than those the Board of Directors have selected to act for Western Farmers in this matter.

We renew our offer to meet with you and receive any suggestions you may have to correct a rail transport monopoly situation that foreshadows the end of what has otherwise been a mutually beneficial relationship. We urge you to join with us in an effort to work out a way to overcome this cancerous monopoly which is eating away at our vital interests.

Very truly yours,

Thomas W. Stevenson
General Manager

cc: F. K. Blackard, President
Triton Coal Company

Senator DECONCINI. Thank you. I take it from that testimony, Mr. Stevenson, that you would consider yourself and your group a captive shipper. Is that fair to say?

Mr. STEVENSON. That is exactly correct.

Senator DECONCINI. And when you had the quote of $11 and something in 1977, was that under a long-term quote or was that to be adjusted yearly, or what was the arrangement?

Mr. STEVENSON. As you know, in those days, it was under the ICC jurisdiction and a contract, per se, was not something that was granted. That was the quoted rate that we understood that we were to get.

Senator DECONCINI. Well, did you have any understanding of how long that would last?

Mr. STEVENSON. We assumed that it would be subject to the typical ICC corrections.

Senator DECONCINI. When the rates more than double over a period of time of, what, 5 years, 6 years, what does the Burlington or any other carrier—what excuse do they give you?

Obviously, you complain, and you holler, and scream, and you ask them to cut that. What do they say? Do they say labor costs? Do they say environmental costs, or what do they tell you?

Mr. STEVENSON. I will say something at risk. I am a certified public accountant and in my career I have had the responsibility of auditing firms and justifying costs of production. And for the life of me, I could not figure it out, and I believe it would take a fleet of people to try to figure it out.

They do not give a good reason. It is basically whatever the market will bear, and we have letters attached to our testimony to that effect.

Senator DECONCINI. Thank you very much.

Mr. Holum, I have asked other witnesses this question and I would just like to pass it by you. In your opinion, why cannot the ICC rule on this issue and grant some relief? Do you think that they are prohibited or are they captive themselves?

Why does not the ICC respond to legitimate complaints that you and other customers have made? Do you have an opinion?

Mr. HOLUM. We have not made complaints to the ICC because we have decided after watching their performance with respect to other shippers that it would be a futile exercise. It is a little hard for me to look inside the heads of the Commissioners at the ICC.

But it is my judgment that they have given entirely too much attention to the Staggers Act when it said assist the railroads in becoming revenue adequate, and completely ignored their responsibility under the Staggers Act to provide a level of protection of the captive shippers. That is unfortunate, but that is the record.

Senator DECONCINI. You used some very strong language in your testimony, going so far as to make some reference to extortion on the shippers here. Obviously, you feel that you are really at their mercy and, in essence, have no alternative. Is that a fair summary?

Mr. HOLUM. When a powerplant has been located—and that is a very difficult job; I was involved very intimately in helping one group site a powerplant—when a powerplant is sited, it finds itself pretty much at the mercy of the railroad that serves between the mine and the powerplant.

As I look at this legislation, I see many advantages, but one that I think is worth underscoring is the advantage to utilities in being able to locate powerplants so that if a mine is located on one railroad and the powerplant is located on another carrier, then at least you have a competing situation between two railroads.

Senator DECONCINI. Thank you very much.

Ms. Watts, did you have some testimony you wanted to give for Mr. Bergland or do you want to wait for him?

Ms. WATTS. No. We have submitted the full testimony for the record.

Senator DECONCINI. OK, fine; thank you.

Ms. Gonze, you have suggested that the rail industry should become—I believe you said this, and correct me—should become a regulated industry once again. Did I misinterpret your statement?

Ms. GONZE. I did not intend to suggest anything of the kind, except insofar as the Staggers Act was written by Congress to continue regulation in monopoly conditions. It was not intended that, in fact, it should be a deregulated industry where captive shippers are concerned.

We would suggest effective regulation under the Staggers Act for monopoly carriers, and we would suggest the injection of competition, as this bill would do, where it does not exist.

Senator DECONCINI. I just wanted to clarify that. You are supportive of the intent of the Staggers Act and of the deregulation. It is this particular captive shippers problem that you believe needs some clarification and direction so that there will be competition?

Ms. GONZE. That is correct. We support regulation in monopoly conditions.

Senator DECONCINI. Has your organization made attempts to have the ICC rule on the rate increase that you spoke of in your statement?

Ms. GONZE. APPA has been involved in virtually every major rulemaking and court case that has been undertaken since 1980—revenue adequacy, market dominance, coal rate guidelines, productivity—through the ICC and through the courts. We have virtually exhausted our remedies at both the ICC and the courts.

Senator DECONCINI. Have you filed any antitrust violations?

Ms. GONZE. APPA is not a utility, but a trade association, and we have not, of course, done so.

Senator DECONCINI. Thank you. I have no further questions. Thank you, ladies and gentlemen, for your very good testimony.

We will now hear from William Dempsey, president of the Association of American Railroads, and Michael Donahue, vice president of coal and taconite marketing and services planning, Burlington Northern Railroad.

Gentlemen, we welcome you. Your full statements will appear in the record. Mr. Dempsey, would you like to lead off?

STATEMENT OF A PANEL CONSISTING OF WILLIAM H. DEMPSEY, PRESIDENT, ASSOCIATION OF AMERICAN RAILROADS, WASHINGTON, DC; AND MICHAEL M. DONAHUE, VICE PRESIDENT, MARKETING AND SERVICES PLANNING, COAL AND TACONITE DEPARTMENT, BURLINGTON NORTHERN RAILROAD, FORT WORTH, TX

Mr. DEMPSEY. Thank you, Mr. Chairman. I am glad to be here to be able to give the views of the association on this bill, S. 2417. Of course, I have got a written statement that I would ask be incorporated in the record.

Senator DECONCINI. Without objection, it will appear in the record in full.

Mr. DEMPSEY. I think I would like to make three points in the brief time available to me. The first is that the subject matter of this bill has been comprehensively dealt with by the Congress under the Interstate Commerce Act.

The second point is that the principle of rate regulation that is reflected in the bill would be ruinous to the rail industry if adopted either by the Commission or by the courts. The third is that, in fact, the Staggers Act has worked fully as intended with respect to protection accorded to captive shippers.

I am sorry, but I was not able to be here; I had to testify in the House, but I understand you have heard a good bit about the Staggers Act already, and so I do not know that I need to elaborate very much on my first point.

The question at stake is who is the captive shipper; that is to say, where is there a monopoly? And then, once the captive shipper is identified, what happens with respect to rate regulation?

It is precisely that issue that has been committed by the Congress to the Interstate Commerce Commission ever since the last century. And as recently as 1980 when the Staggers Act was enacted, Congress canvassed the whole field again and adopted the principle that there should be deregulation of the industry to keep it from going even more on the rocks than it was, but that at the same time there should be protection accorded to captive shippers.

The collision, then, it seems to me, between the Interstate Commerce Act and the proposed bill is clear. One could envision a situation in which the railroad would be held to have charged reasonable rates by the Interstate Commerce Commission and the courts under the Interstate Commerce Act, but held liable for treble damages or possibly even criminal liabilities under the Sherman Act.

Second, the principle of rate regulation that is reflected here is one that would eliminate what we call in the industry "differential pricing" in favor of what one might call average cost pricing. The idea, to put it in a very rough way, is that in lieu of differentially pricing rail services all shippers ought to be treated essentially the same; that is to say, if we charge one shipper a rate that, in our parlance, comes to, let us say, 150 percent of variable cost, we ought to charge all shippers essentially or substantially the same rate.

The principle of differential pricing has been recognized by the Commission as essential to the well-being of the industry and to captive shippers for decades. The reason is simply this: About 85

percent of our traffic is competitive traffic—that is, competitive with trucks and with barges.

So we do not have rate freedom there; we are governed by the marketplace. If we can get traffic from the highways or from the waterways by charging a rate that does not cover our fully allocated costs, but that does cover something more than our variable costs on that movement, then that competitive traffic is making a contribution toward covering our fixed costs, which are very high in our industry.

Now, if we could not do that, if we had to charge the competitive shipper the same as we charge so-called captive shippers, thereby driving the competitive traffic off the railroads, onto the highways and onto the waterways, the full burden of those fixed costs would fall on the captive shippers.

Therefore, the principle of differential pricing is essential to our well-being and essential, really, to the economic welfare of the captive shippers; and it has always been recognized as essential by anyone who has looked at the industry from an economic and marketing point of view.

Finally, what has happened to captive shippers, in fact, under the Staggers Act? Let me just take coal since that is the commodity we hear most about.

What has happened to coal rates under the Staggers Act is hardly anything. We have had under the Staggers Act the right, without investigation or suspension, in the last 44 months to increase coal rates 22 percent over inflation. In fact, we have increased coal rates over inflation less than 3 percent.

The rate of increase in coal rates since Staggers has been roughly half of the rate of increase in coal rates before Staggers.

Senator DECONCINI. That is on a national average?

Mr. DEMPSEY. That is on a national average. These are not my figures, let me say.

Senator DECONCINI. Yes.

Mr. DEMPSEY. But it is on a national average, of course.

Senator DECONCINI. Well, excuse me.

Mr. DEMPSEY. Yes.

Senator DECONCINI. Well, how do you resolve Mr. McKeever's testimony of Western Coal Development Co., where he cites in his testimony, with respect to CP&L, the original rate quoted in 1977 was $13 a ton from Colowyo to Coleto Creek station, and when shipments started at the end of 1979 the rate imposed by D&RGW was $20.85 a ton, a 60-percent increase in 2 years?

The rate is now $29.93 a ton, an increase of 130 percent over the quoted amount at the time of the contract. Now, that is a little bit more than any inflation could possibly be assumed. How do you resolve that kind of testimony, unless it is wrong?

Mr. DEMPSEY. Well, the only way I can resolve it, obviously, unless my colleague can, is to go to the D&RGW, and I would love to do that and give you a supplemental statement dealing with that.

Senator DECONCINI. I would love to have it.

Mr. DEMPSEY. Yes, but, clearly, there will be instances that do not comport with the national average.

Senator DECONCINI. Clearly, yes. [Laughter.]

Mr. DEMPSEY. Well, there will be. There are circumstances that warrant increases in coal rates, such as major capital investments.

Senator DECONCINI. But you would not want to attempt to justify this one?

Mr. DEMPSEY. I certainly do want to attempt to justify that one, Mr. Chairman.

Senator DECONCINI. You do?

Mr. DEMPSEY. Of course.

Senator DECONCINI. I really welcome hearing your written testimony to justify a 130-percent increase. Thank you. Go ahead.

Mr. DEMPSEY. One final word. Most of the complaints that we hear about are complaints based upon apprehension of what may happen, and most of them center upon the proposal of the Interstate Commerce Commission that, among other kinds of principles to be applied in regulating coal rates, there be a cap of increases of 15 percent a year above inflation.

What then people do quite earnestly, and I understand their concern, is to say, well, for goodness sake, is that what is going to happen? Are we going to have increases in coal rates of 15 percent a year over and above inflation? And if so, look how high they will go.

Well, I say two things about that. One is that the experience that I have just recited to you under the Staggers Act indicates that it is absolutely and utterly impossible for the railroads to take any kind of increases like that. And for that reason, and because this has caused such apprehension, we join the coal industry and the utility industry in opposing that guideline.

While one can scarcely predict with confidence the outcome of one of these proceedings, I have, I must say, absolute confidence that that part of the proposed coal rate guidelines will not be in the final order of the Commission.

I think that is all I have right now, Mr. Chairman.

Senator DECONCINI. Thank you, Mr. Dempsey. I just have to comment also that Mr. Stevenson testified here just a few minutes ago that from 1977 to 1984, the shipping costs went up there per ton from $11.94 to $23.69. That is not anywhere in the range that you are talking about, 15 percent.

Mr. DEMPSEY. It is not.

Senator DECONCINI. I know you are talking about national averages, but we are talking about specific geographic areas that, to me, it is just as evident as can be that the railroads are gouging the shippers. Consequently, people in Detroit and Chicago who have to rely on that coal are paying an exorbitant amount due to the greediness of a few railroads who do not care.

I just cannot believe that you would sit there and not want to come before us and say, by gosh, we not only will justify this; we are going to make some explanation and hopefully moderate our outrageous increases that we have granted in these specific areas.

Mr. DEMPSEY. Well, I might rephrase that just a little in making that response, but certainly we want to justify whatever we have done in the coal rate area. And those cases that you point to—I assure you, I will get the relevant data from our perspective and give it to you.

I guess the first question I would have, since we are talking about essentially whether the Staggers Act is working, is whether complaints have been filed in those cases, and if so, what has happened to them.

Senator DECONCINI. Well, even if there have not been complaints, if you have these kinds of increases, unless you have got some marvelous justification, and I look forward to it, it seems to me that the railroad industry surely has a conscience. They are good corporate citizens; they have done great things in my State. They have been generous contributors to many philanthropic things.

I would think that they would have a conscience as to such tremendous increases.

Mr. DEMPSEY. Well, let me just say one point. Well, perhaps I should not; I think I will leave it. I was going to mention the letter that has been sent to all of the interested coal companies and other interested parties by the president of the Burlington Northern.

Is that part of your testimony?

Mr. DONAHUE. Yes.

Mr. DEMPSEY. I am just going to leave that for the Burlington Northern representative.

Senator DECONCINI. Fine. Mr. Donahue?

STATEMENT OF MICHAEL M. DONAHUE

Mr. DONAHUE. Thank you very much, Mr. Chairman. I appreciate your invitation to testify before this committee on S. 2417. During my 30 years of railroading—a career which began as a section laborer and a switchman in Montana—I have never witnessed such dynamic, positive changes as we are now experiencing in rail transportation.

These changes are resulting from innovations possible through the Staggers Act. Mr. Chairman, quite frankly, S. 2417 would be, in my estimation, a circumvention of the Staggers Act. It imperils incentives that have permitted all this progress.

I have worked through many changes within railroading, but the Staggers Act is different. It has changed the nature of our enterprise from simply running trains to operating a business.

With the Staggers creation, Congress did its work well in 1979 and 1980 with its vision. Staggers is working for the majority benefit of our consumers, shippers, as well as the railroads. In 3 years, we have witnessed massive changes from green eyeshade days to competitive, market-oriented business.

In my opinion, calls for legislative change ring hollow against facts compiled in this post-Staggers timeframe. First, after the initial adjustments in BN coal rates, we now expect to hold the line to inflation and cost increases.

Second, BN grain rates actually are lower now than 4 years ago in constant dollars. Third, nearly half of BN's coal, fertilizer, export grain, clay, sand, and chemicals move under agreed-rate contracts. Few people would have believed that this half of our business would be mutually negotiated to contracts within 3 years.

Fourth, BN policy is to continue negotiating these win-win contracts with our customers who desire a contract. Fifth, our future

is starting to be more secure and BN's investment dollars are at a historic high—$539 million in 1982, all the way up to $679 million budgeted for 1984.

Sixth, no longer do we have questions about deferred maintenance, car shortages, or impending bankruptcies. Most complaints about the Staggers Act seem to be coming from Washington, DC, rather than from our customers, and are focused on the ICC rather than on our railroad.

ICC regulations are not in concrete. They can be, and are being negotiated by industry and shippers. As an example, on August 15 of this year, Walter Drexel, our chairman, wrote a letter disavowing the 15-percent coal increases proposed in the ICC guidelines.

The complaints we are handling are principally pre-Staggers. Let us look at BN's pre-Staggers section 229 cases. The vast majority have already been settled by shipper-railroad negotiation. Only 4 of our 20 coal cases remain. All 36 of our grain cases have been settled.

The other coal cases that the public hears about, our so-called letter-of-intent cases, are not typical of post-Staggers patterns. Despite the difficulty of these cases, we have and are and will continue to attempt good-faith negotiations of even the most difficult.

Again, I say the great majority of our customers are satisfied. In conclusion, railroad efficiency has improved. Management has responded to the challenge of rebuilding this industry.

While we have made some upward rate adjustments, our progress has been derived from increased productivity, not abuse of our markets. BN is working to be a partner with its shippers. In my opinion, S. 2417 assumes a hostile relationship and would institutionalize it.

In summary, Mr. Chairman, S. 2417 is, at best, premature. We have made great strides in 4 years within our industry and within Burlington Northern. Please, let us continue.

Thank you.

[The prepared statement follows:]

Statement of William H. Dempsey,
President of the Association of American Railroads,
Before the Senate Committee on the Judiciary

September 18, 1984

I appreciate this opportunity to express the views of the Association of American Railroads on S. 2417, a bill "To amend the Sherman Act to prohibit a rail carrier from denying to shippers of certain commodities, with intent to monopolize, use of its track which affords the sole access by rail to such shippers to reach the track of a competing railroad or the destination of shipment."

S. 2417 would create an antitrust remedy in an area of commerce as to which the Congress has already created a comprehensive, consistent and exclusive regulatory structure. While directed to the Sherman Act, the effect of the bill would be to amend the Interstate Commerce Act and thus create wholly inconsistent statutory objectives. However it is to be characterized, I can tell you at the outset that it would sound the death knell for our privately-owned railroad system. And it would do so in response to complaints that railroads are overcharging some classes of shippers that are simply unjustified as a matter of fact, as I shall indicate.

As the Committee is aware, the bill would make it unlawful for a rail carrier, with intent to monopolize, to deny the use of its track on what the bill deems "reasonable terms" to a shipper of coal, ore, grain, forest products, chemicals or fertilizers if that track is the only rail connection with a competing rail carrier or to the destination of the shipment.

An intent to monopolize is to be conclusively presumed from a denial to the shipper of the use of the rail facility on the "reasonable terms" set forth by the bill and the failure to permit other rail carriers to use the facility to transport the shipper's goods.

The basic purpose of the bill is to regulate maximum rates. Senator DeConcini made this clear when he introduced the proposal, explaining that the bill "would amend the Sherman Act in a manner which would assure captive shippers fair and reasonable freight rates for the transportation of their product." Cong. Rec., March 13, 1984, S. 2624. At the heart of the provisions as to maximum rates, the bill provides that the railroad's terms are unreasonable if its rates are higher than the level necessary to yield a fair return on the proportion of the carrier's investment which the shipper's traffic bears to all traffic using the railroad facility.

As this discussion makes clear, while S. 2417 employs antitrust terminology -- monopoly and intent to monopolize -- and creates a new per se antitrust violation enforceable by shippers against railroads in certain situations, antitrust is not really what S. 2417 is all about.

What S. 2417 really concerns is maximum rate regulation. At root, it is an attack on the concept of "demand" or "differential" pricing of rail services and the standards for determining the maximum reasonableness of rail rates. The absolute need for differential pricing of rail services and the need for regulation of rail rates where the forces of competition are an insufficient constraint on rail rates were explicitly recognized and dealt with by the Congress in the Staggers Rail Act of 1980, which was the latest amendment to the Interstate Commerce Act. I would like to review the ways in which the Interstate Commerce Act, as amended by Staggers, deals with these issues of competition and rate regulation and then come back to the ruin that would result from S. 2417's proposed outlawing of differential pricing.

A comprehensive and exclusive statutory scheme for regulating rail rates and for compelling a railroad to permit the use of its facilities by another in situations where that was appropriate was completed with the Transportation Act of 1920.

With the Railroad Revitalization and Regulatory Reform Act of 1976 and the Staggers Act of 1980, the Congress loosened the reins on ratemaking that had been applied in that earlier era of our economic life, but it did not remove them, While recognizing that reasonable rates for rail transportation should be set by "competition and the demand for services" to the maximum extent possible, the national policy reformulated in the Staggers Act also recognized as an objective of regulation the need "to maintain reasonable rates where there is an absence of effective competition and where rail rates provide revenues which exceed the amount necessary to maintain the rail system and to attract capital."

The concept of limiting the Interstate Commerce Commission's jurisdiction to regulate the maximum reasonableness of rates originated with the 4-R Act of 1976. It limited the Commission's jurisdiction to instances where the rail carrier was shown to have "market dominance," which was defined as an "absence of effective competition." The Staggers Act further modified the definition of market dominance to remove from the Commission's jurisdiction rates which yielded a revenue-to-variable cost percentage below a prescribed threshold -- currently 175 percent.

As a result of these two amendments to the Interstate Commerce Act, the Commission now has jurisdiction to determine the reasonableness of any rail rate where the yield from that rate is above 175 percent of variable cost and where there is an absence of effective competition. In assessing the absence or effectiveness of competition the Commission looks at all aspects of competition -- intramodal, intermodal, product and geographic.[1/]

1/ These terms are used to mean, respectively, competition among railroads, competition between a railroad and another mode of transportation, competition arising from the substitutability of products, and competition arising from the availability of the same product from different sources or the ability to ship the product to different destinations.

Thus, while there has been deregulation of rail rates where those rates are found to be effectively constrained by competition, there has been no deregulation of rates where the Commission finds an absence of effective competition.[2/] In that circumstance the Commission retains the exclusive power it has always had to prescribe maximum rate levels. It is important to note in this respect that the amendments effected by Staggers require the Commission in determining the maximum reasonableness of rates to consider the revenue needs of the rail carrier. This admonition sprang from the fact that between 1970 and 1979 22% of the railroad industry had gone into bankruptcy as a result of years of inadequate earnings. The Congress realized that if the railroad industry were to survive in the private sector it could no longer be used as an instrument of national policy to subsidize other industries or regions. It had to be regulated in accordance with sound economic principles. At the very least that meant that over the long run the railroads had to be allowed to earn adequate returns on the capital invested in the business. The Commission will soon hear oral argument in a proceeding to establish an objective maximum rate standard for coal that is economically sound, fair to shippers and sensitive to the need for railroads to attain adequate revenue levels. Moving from the old subjective standard of "reasonableness" that largely ignored the railroad industry's long-run revenue needs to an objective economic standard of reasonableness is not easily done. We will have to wait and see what the current proceeding ultimately yields.

2/ In conformity with this principle, before the Commission may completely exempt a type of service from regulation pursuant to its authority under 49 U.S.C. 10505 it must find with respect to that service that regulation "is not needed to protect shippers from the abuse of market power."

The point I wish to stress with respect to S. 2417 and the concerns of this Committee is this: The bill under consideration deals with situations in which a shipper has access only to a single railroad -- where the shipper is "captive," in popular parlance -- and would set ratemaking standards for those situations.[3/] But the Congress has for decades entrusted regulation of rail ratemaking to the Interstate Commerce Commission, and as recently as 1980 enacted a comprehensive reform of the regulatory system dealing precisely with the subject of S. 2417 -- the standards to be applied in determining which shippers are "captive" and in determining the lawfulness of rates charged to such shippers. Thus there is no lacuna to be filled by the antitrust laws. Rather, the remedies afforded by the Interstate Commerce Act are plainly exclusive. It would be grossly unfair to enact a measure under which a railroad, having successfully established before the Commission and the courts that its rate to a "captive'shipper was reasonable under the Interstate Commerce Act, could then be compelled to pay treble damages to that shipper pursuant to a finding that the rate was unlawful under the antitrust laws.

The bill is at odds with existing law in still another respect. It deals not merely with rates, but with trackage rights, another subject that has been dealt with by the Congress in the Interstate Commerce Act. For example, section 11103 of Title 49, U.S. Code authorizes the Commission, upon certain findings, to require a rail carrier to permit another carrier to use its terminal facilities. It also authorizes the Commission to require carriers to enter into reciprocal switching agreements by which carriers gain access to shippers on each other's lines. Section 10901 expressly authorizes the Commission to resolve

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3/ It is to be noted that the bill is fatally flawed under economic and antitrust analysis because it ignores the availability of non-rail transportation and other economic constraints on rail pricing decisions which are frequently, if not inevitably present in the situation addressed by the bill.

disputes between railroads where one proposes to build a railroad line across the line of another. And the Commission has for years construed its general authority to condition its approval of mergers (section 11344) to include the condition that trackage rights be granted to other carriers where that is deemed necessary for competitive reasons.[4]

The instances in which the facilities of one railroad can be required to be made available to another are thus limited by statute -- and for good reason. That reason has to do with the cost structure of a railroad and the competition it faces for most of its business. It is these factors which also dictate the differential pricing of rail services. As I noted earlier, S. 2417 is in fact an attack on differential pricing which, if successful, would preclude the viability of the railroad industry in the private sector. I would like to explain why this is so and why there is a nexus between differential pricing and the use of railroad facilities.

Differential pricing is the pricing of each service in relation to the demand for that service. Such pricing is economically beneficial because it lowers the price of rail transportation for all shippers by encouraging the purchase of more service by shippers with a low demand for rail service. The ability to price differentially is essential to the railroads because they face strong competition for most of their traffic. Because of that competition, the revenues derived from the traffic are often not sufficient to cover both the variable and fixed costs attributable to the movement. Variable costs are costs (such as fuel) which would not be incurred except for the fact of the movement of particular traffic. Fixed costs are costs (such as roadbed) that exist independent of the movement of particular traffic. The variable costs plus an allocated share of fixed costs constitute

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4/ These are not empty powers but have been invoked by the Commission on many occasions. (D&H Railway Co. v. Conrail -- Reciprocal Switching, 366 I.C.C. 718 (1983); Mid-Tech Paper Corporation et al. v. Chicago and Northwestern Railway Co; I.C.C. Docket No. 39021, not printed (September 19, 1983).

the "fully allocated" costs of the movement (which costs include the cost of capital). Because the fixed costs are being incurred whether or not particular traffic moves, anytime the revenues from a traffic movement are sufficient to cover variable costs and make some contribution to fixed costs the traffic is desirable. The higher the degree of competition for traffic, the lower the revenue in excess of variable cost (and, hence, the lower the contribution of that traffic to fixed costs). The differential pricing of rail services is, in effect, the quantification of that inverse relationship.

The achievement of revenue adequacy for a railroad, or any other business, requires that over the long run it recover its full costs -- variable and fixed. Given the inability of railroads to recover their full costs from unregulated competitive traffic, the objective of a maximum ratemaking standard must be to regulate the rates on non-competitive traffic in a manner that is fair to the shipper who is dependent on rail service but still allow the carrier the opportunity to cover its full costs.

Differential pricing is not unfair to any shipper. Those shippers who are truly dependent on rail service -- the so-called "captive" shippers -- must ultimately be responsible for covering the full costs of the rail service they say they need. The argument advanced by some "captive" shippers that, because of differential pricing, their traffic subsidizes the competitive traffic is simply not true. To the contrary, to the extent competitive traffic makes any contribution to a railroad's fixed costs, that traffic is benefitting the "captive" shipper by reducing the amount of fixed costs that must be covered by rates on captive traffic.

Nor is differential pricing in the railroad industry something new. It has existed since the dawn of the railroad industry and has been long accepted as a necessity by the

Interstate Commerce Commission. As noted earlier, the rail transportation policy enunciated in Staggers was to allow competition "and the demand for services" to establish reasonable rates. The need for differential pricing was also implicitly recognized in the report of the Committee on Conference which observed that "All shippers as well as the carrier are better off if traffic which makes a contribution moves than if it does not, because the carrier is made financially stronger and need not rely as much on revenue from other shippers." (Report No. 96-1430 at 90)

Let's look now at how the need for differential pricing and the grants of trackage rights are interrelated. If the railroads were compelled to grant trackage rights wherever necessary to permit a shipper to be served by at least two railroads, it would be unlikely that any railroad could recover the fully allocated costs of the service it was providing. This result would follow because the introduction of competition for the formerly "captive" traffic would tend to drive the rates on that traffic down to or below the level of fully allocated costs. With no traffic moving above fully allocated costs, and most traffic moving below that level, it would only be a matter of time before a railroad went out of business or, if the past is any indication, became the object of federal assistance.

The only way a railroad could possibly survive under such a "forced competition" regime would be if the price for granting trackage rights were set high enough to fully compensate the railroad. And that point brings us back to the real purpose of S. 2417. Under section 9(a)(2)(C) of the bill, the most a railroad could charge for the grant of trackage rights would be a rate that yielded "a fair return on the proportion of the rail carrier's prudent investment in the railroad facility that the shipper's traffic bears to all traffic using such railroad facility."

Under that formula, the greater the amount of competitive traffic a railroad carried (which traffic would reduce the over-

head burden otherwise allocable to the "captive" shipper), the lower the rate chargeable to the "captive" shipper for trackage rights. Assuming that most of the competitive traffic was moving at rates below fully allocated costs, which would likely be the case, a carrier could never recover its full costs. It could only recover full costs on that portion of assets equivalent to the "captive" shipper's portion of total traffic. This formula would not remove a cross-subsidy but it would create one. The railroad stockholder would be called upon to subsidize the "captive" shipper.

Against this background the proposed legislation is neither necessary nor appropriate. There is no need to single out the railroads for special sanctions under the antitrust laws.[5/] The railroads are already subject to the antitrust laws except to the extent that they have been preempted by the regulation which Congress, through the statutes mentioned above, has provided. Over the years the Congress, the Courts and the ICC have carefully harmonized the interplay between the antitrust laws as a whole and the extensive regulatory scheme governing railroads and there is no demonstrated need or reason to upset this balance.

If there are concerns about certain areas of railroad regulation, they should be addressed within the regulatory context, giving full consideration to all of the complicated, economic issues, and not by asking the Courts which are neither specially trained nor equipped to resolve those issues -- to act as super regulators under the antitrust laws.

The inappropriateness of the proposed legislation is compounded by the fact that it would seek to resolve perceived (but we submit overstated and in some cases non-existent) problems by turning them over to the Courts rather than the administrative

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5/ It is to be noted that these sanctions embrace criminal penalties as well as civil remedies. For rates found reasonable under the standards of the Interstate Commerce Act, a railroad could be subject to criminal prosecution.

body which Congress created for the purpose of regulating railroads and which has done so for nearly 100 years. There is certainly no demonstrated necessity for so drastic a step. And one result -- the shifting of workload from the Commission to the courts with increased probability of inconsistent decisions -- is certainly not a desirable public policy objective.

Rail regulation was entrusted to Congress by the ICC because Congress recognized that the economic complexities of a sound national rail transportation policy were such that its administration required a special expertise that the Courts do not possess and should not exercise as a matter of initial jurisdiction as opposed to a forum to appeal agency actions. That is still true. We recognize that there have been concerns recently expressed regarding Commission actions. However, to the extent these concerns have merit (which we do not concede) they should be addressed within the regulatory framework, not by enacting a special railroad section of the antitrust laws which is not framed to give full consideration to the special needs and complexities of a sound, long-term rail transportation policy.

Finally, the proposed legislation overlooks substantial Constitutional problems, in the form of the taking of private property. As noted above, the basic thrust of the proposed legislation is to compel a railroad, in effect, to turn its trackage and facilities over to virtually any other competing railroad selected by a shipper on broad and ill-defined terms that by no means assure just and adequate compensation. No other industry is required to turn its physical plant over to its competitors at the whim of a single customer. The operational problems posed by any system of unlimited trackage rights, such as the proposed legislation suggests, are substantial. To the extent it is defined, the compensation formula proposed by the bill would appear to fall well short of Constitutional requirements that

apply when private property is appropriated by legislative fiat. Fair and just compensation under the Constitution is measured by the fair market value of the appropriated property which in the case of operating property, such as here involved, would be measured by the capitalized value of the revenue that the property is producing at the time of the taking. That is clearly not the compensation standard that the proposed legislation contemplates and, as such, it would appear to run afoul of the Constitution.

To summarize, S. 2417 deals with matters embodied in the Interstate Commerce Act and not with matters embraced by the anti-trust laws. It is an effort to repeal by indirection the maximum rate regulation aspects of the Interstate Commerce Act. And it ignores the fact that the Interstate Commerce Act constitutes an integrated, and with respect to maximum rates and compulsory facility use, an exclusive statutory scheme. So long as the maintenance of an economically viable and privately-owned common carrier rail system remains a national objective, we should resist efforts to tamper with the elements of the statutory construct for that system while ignoring the effects on the whole.

Leaving aside the legal and legislative issues raised by S. 2417, do the supporters of the bill have a valid complaint which the Congress should address in some fashion? Have the railroads as a result of the Staggers Act amendments taken unreasonable rate increases? The fact is that they have not.

If we look first at coal rates, which are the point of most contention, we find that since October 1, 1980, those rates have increased only 2.7 percent in constant dollars. In other words they have been increased only slightly more than the rate of inflation.

If we look at the rate increases since October 1, 1980 on all commodities carried by rail, we find that the rate level rose only .4 percent in constant dollars. The rate levels for four of the eleven leading commodity groups actually declined during that

period. The largest increase during that period was for lumber (4.9 percent) and the largest decrease was for transportation equipment (4.3 percent).

Looking at the coal rate issue in more detail, we find that in 1983 coal accounted for 22 percent of all railroad revenue but 38 percent of all tonnage. In terms of revenue per ton, coal ranked 15th among the top 18 commodity groups. In terms of revenue per ton mile, it was in 18th place. By any measure, coal is not bearing a disproportionate share of the cost of building, maintaining and operating our national railroad system.

If we compare rail coal rates with the price of coal, we find that coal prices shot up 77 percent over their 1972 level in constant dollars during the oil crisis period 1974-75. From that peak they had declined by 1982 to a level only 32 percent higher in constant dollars than the 1972 level. Rail coal rates, on the other hand, actually declined slightly during the 1970's and by 1982 were still 1 percent below their 1972 level in constant dollars. Of course, in its comparisons the coal industry likes to focus on the post-1975 period because that shows a declining trend in coal prices and a (slightly) rising trend in rail coal rates. All they ask is that the observer forget the 77 percent constant dollar leap in coal prices in 1974-75 which the softening energy market would simply not sustain.

In conclusion, I urge the Committee to take no action on S. 2417. It does not raise a legitimate antitrust issue and is unsupportable on the merits of the transportation issue it actually addresses. I also request the opportunity to supplement this testimony as necessary to respond to issues raised by other witnesses.

I will now be happy to answer any questions the Committee may have.

TESTIMONY

Michael M. Donahue

Burlington Northern Railroad

Senate Judiciary Committee

September 18, 1984

Good afternoon Mr. Chairman. I am Michael M. Donahue, Vice President for Marketing and Services Planning, Coal and Taconite Department, Burlington Northern Railroad of Fort Worth, Texas. I appreciate your invitation to testify before this Committee on Senate Bill S. 2417.

We at Burlington Northern and our shippers have been doing business for nearly four years under the provisions of the Staggers Act. Our world has changed enormously since enactment, and that process of change is continuing. We are learning more about the marketplace, trying out new ideas and working to stay ahead of our competitors. We are working with customers to understand their transportation needs and problems, and we are adjusting our service and rates to respond to those needs. We are investing in our railroad at historically high levels: we now have confidence in our future, and we want to serve our customers with the best transportation that our ingenuity can provide.

Naturally, when we see a proposal such as S-2417, and other re-regulation bills, we become concerned about losing the productive and stimulating business environment that has benefited our customers and us. In the face of these surprising proposals we have taken time for some introspection; we have asked ourselves during this period of fervor and excitement, have we overlooked something or someone? Have any of our customers been damaged in some way?

The answer is that the great majority of our customers are indeed satisfied with the changes that Staggers has wrought, that they are benefiting from the relaxed regulatory system introduced in 1980. Of course, we all have had to make adjustments, shippers and carriers alike, in the wake of a sweeping reform like Staggers -- but for the most part

those changes are behind us, and all of us are benefiting from the efficiency and spirit of a reborn industry.

What we did find -- and I think you will find this especially interesting -- is a concern among some shippers for the future, specifically a concern that the ICC would no longer protect them from traditionally perceived railroad abuses. The comments, Mr. Chairman, published in the Congressional Record on March 13 of this year, when the bill was introduced, illustrate the point well. Those comments refer extensively to the ICC's proposed maximum rate standard for coal, which among its provisions allows for a 15% rate increase over inflation each year, until the rate meets another limit, or until the railroad earns adequate revenues. The proponents of this legislation note that this "system of nationwide rail rates will result in a doubling of already high present rates within five years." While the mathematics in that statement are correct, the premise and the prognosis are not.

I know of no circumstance under which our railroad company could invoke such increases -- the market would not permit it -- we would simply lose the business. Competition in the coal business is acute. Not only are railroads competing for coal traffic, but mines served by differing transportation companies compete among themselves for contracts.

In that connection I would offer some independent judgments on the question from outside the transportation industry. This past summer ICF, one of the most respected and most independent firms engaged in the business of energy analysis, completed a study for the Environmental Protection Agency which dealt with transportation rate assumptions for use in coal market forecasting. This is precisely the issue, of course, behind the current Staggers debate. The report notes:

> Railroad ratemaking gained considerable flexibility under the 4-R Act of 1976 and gained momentum with the passage of the Staggers Rail Act in 1980. As the railroads have moved further into a deregulated environment, there have been increasing opportunities to observe rail-

> road pricing behavior relative to the conceptual arguments presented earlier.
>
> Although many rail movements have shown substantial changes (both up and down), there is little evidence to suggest that deregulation is leading to widespread increases in rail rates above the underlying costs. . . . Between 1977 and 1983, costs rose at an average annual rate of 9.3 percent, while rates rose at a 9.7 percent rate. Since the passage of the Staggers Rail Act in October 1980, railroad costs have increased at a 6.8 percent annual rate, while rates have increased at a 6.6 percent annual rate. (Emphasis added.)

The report then concedes that even if one argues with the computation of the railroad cost basis, the "increase in real rates over costs is still well below levels permitted under the Staggers Act and subsequent rulings."

The president of a major natural resource corporation in the coal business wrote in reference to the ICC's rules on rate making:

> The new rate setting flexibility, when combined with the opportunities for western and eastern railroads to develop and serve the new markets caused by the "freedom of choice" policy, should engender considerable price competition and resultant lower rail rates. In fact, there have been several prominent examples in recent months of railroads reducing rates to remain competitive.

These unbiased, unsolicited comments reflect clearly the market environment faced by our industry.

Quite frankly the ICC's 15% provision has been of no use to us (nor any other railroad I know of) and, because it has raised unwarranted fear among shippers, it has been a decidedly negative factor in our business. I have attached a letter which was sent to all of our coal customers on August 15 by our chairman, Walter Drexel, disavowing any intent to use this rate increase provision. We are testifying to that point in the ICC hearings today on coal rate standards.

Mr. Chairman, I began by commenting on the changes that have occurred and still are occurring in the railroad transportation business. The Drexel letter and the ICC hearings represent other aspects of change: a growing railroad-shipper dialog, and the evolving process of adjustments in the ICC's interpretation and administration of the Act.

A hallowed principle of governance known as subsidiarity maintains that the most capable organization nearest the problem is the entity that ought to solve it. It seems to me, that is precisely the principle that is at work, outside of the Congress. Nothing we have seen in the record to date suggests that the intervention of this heavily burdened legislative body is necessary. The work you completed in 1980 with passage of Staggers remains sound in concept and practice. Where there are fears or misunderstandings about the future, it is well within the power of those parties concerned -- if they truly seek to reconcile their differences -- to reach a good faith understanding.

Thus, I believe S. 2417 is a remedy searching for an ill. Without getting into details on the form of the remedy, I suggest that this legislation raises serious questions of costs, safety and equity, if not legality.

Now I would like to examine some of the misunderstandings that appear to underlie this proposal. Most important is the premise that competition in the free market has failed to control freight rates, particularly in coal. There is particularly vigorous bidding for coal transportation contracts in the U.S. Burlington Northern has won some and lost a few. The effect of this competitive dynamic is a powerful constraint upon our rates. Non-contract rates for bulk commodities were set by committee and were usually the same for common points of origin and destination, before Staggers. Collective rate-making was prohibited by Staggers, and in the bulk handling business, rail to rail, truck and barge competition is holding rate increases to quarterly inflation based hikes.

In the past few years, we had to raise some non-compensatory coal rates to remunerative levels as a matter of sound business practice. Those rates generally were so low, no competitor would have come close to them in a bid because they were money-losers.

Today, nearly half of our coal movements are under contract and we expect this percentage to grow. (Four years

ago, we had none.) This means that in each of those instances we reached a mutual rate and service package to the shipper's satisfaction in arms length bargaining. No coercion, no government involvement, just a straight forward business agreement, freely contracted by both railroad and shipper. Half of our fertilizer, clay, sand and export grain business and 40% of our chemicals move under contract -- with growth potential for even higher fractions. Our policy is to establish a "win-win" environment, and to negotiate, wherever we can, agreed rates through contracts with our customers.

We have been able to meet rate competition successfully because, through the Staggers reforms, we now have the incentives if not the imperative to compete. Our productivity gains over the past several years have enabled us to hold overall rates well below inflation since 1980 and still invest in the railroad at record levels. (Coal rates, however, increased in the first years after enactment reflecting prior massive investment in our coal hauling lines, and adjustment of non-compensatory rates. We intend that future increases will be in line with inflation and cost recovery levels.) Our grain rates in Nebraska, Montana and North Dakota declined with the introduction of unit trains and have decreased in constant dollars since then. To garner other savings we have worked out fertilizer back haul rate savings for shippers in North Dakota and Minnesota, and alumina back haul rates for shippers in Montana and eastern Washington, using grain train equipment.

One of the more innovative, cooperative productivity ventures with our customers was the formation of our grain car pool. In 1982 grain cars owned by our shippers were in substantial surplus. We were wasting car miles by routing them empty from one facility to another at the owners' request. By pooling these cars, we have reduced empty car movements and put shippers' cars to work on a more efficient, paying basis. This was a sensible and fair solution to a

problem that troubled both Burlington Northern and our private grain car owners.

A final note on settling regulatory issues at the lowest level: the Staggers Act allowed shippers to lodge complaints against rates in effect when these reforms were enacted. Of 20 such complaints on BN coal rates, all but four have been settled; and all 36 grain rate cases were settled through negotiation between BN and its shippers.

In past months railroad companies have been involved in cancelling some of their joint rates -- often characterized as "closing gateways", a misnomer. To state it briefly, between 1981 and 1983 railroads cancelled countless joint rates. Under the Staggers Act, differing routes are priced competitively, and to manage the rate making burden, only those routes that were cost competitive and geographically efficient could be maintained. In some lines of business -- grain for example -- rather than cancel joint rates, we simply lowered our single line service rate to make it more competitive. Generally, we have attempted to preserve routing alternatives for our shippers though we strive to maintain our single line or longer haul routes at the lowest possible rate level.

More recently, the pendulum has begun to swing in the direction of reestablishing certain joint rates. Examples include the Voluntary Coordination Agreement between BN and the Grand Truck Lines, as well as reinstatements between BN and Santa Fe, Norfolk Southern and Seaboard System.

I would add that we are working assiduously with our industry and with our shippers to develop an acceptable standard for ICC review of joint rate cancellations. I believe we have every chance for success in this effort.

Reciprocal switching -- agreements to deliver cars from one railroad to a customer on another within a defined industrial area -- also has been topical in recent months. BN policy has been to seek agreements with other rail companies on an economically sound basis which preserves the maximum

feasible access for shippers to competitive railroads. Thus, we have not cancelled any of our switching agreements.

To conclude, Mr. Chairman, in 1980 the Congress told our industry to get out into the market place and compete. We did so and we are competing. Today I am reporting to you that Staggers is working and the market place is a fairer and firmer regulator of business than a government agency. Someday a change in the legislative environment may be warranted. But there is no evidence to date that S. 2417 or any similar proposals are necessary or desirable, or will be in the foreseeable future.

Walter A. Drexel letter to
Burlington Northern coal
customers

Attachment to M. M. Donahue
testimony of September 18, 1984,
before Senate Judiciary Committee

August 15, 1984

(address)

Dear Mr. (name):

It occurred to me it might be helpful to you and your associates if you clearly understood the Burlington Northern Railroad's position with respect to the Interstate Commerce Commission's proposed coal rate guidelines that would permit railroads who have not attained revenue adequacy to increase coal rates in the future up to 15 percent per year over and above inflation or cost-related increases.

We have reviewed and studied the proposed guidelines in detail, and after doing so are firmly convinced that the proposed annual 15 percent increase authority is excessive and unwarranted. We accordingly have no intention of implementing increases of that magnitude, even if the Commission should adopt such a policy in the future. To the extent that increases over and above inflation and cost-recovery levels are desirable to assist railroads in achieving revenue adequacy, we believe that a much lower limit is more appropriate.

Furthermore, in the absence of extraordinary circumstances, we believe that the current rates established by tariff or those currently under negotiation, or those that may be established for future movements, should be subject only to the Staggers Act or a similar escalation system that adequately meets inflationary needs. Where we have entered into Section 208 contracts under that provision of the Staggers Act, the terms of those contracts will, of course, govern.

We think it important to share our thoughts with you on this matter which affects our mutual interests. If you have insights which you would also like to share with us on this subject, please let us know. In the meantime, I wanted you to know that Burlington Northern Railroad intends to urge the Interstate Commerce Commission to modify its proposed guidelines in a manner that will more closely reflect the views expressed in this letter.

Very truly yours,

Walter A. Drexel

cc: Chairman Reese Taylor, Jr. - ICC
ICC Commissioners

QUESTIONS SUBMITTED BY SENATOR DECONCINI

Question No. 1:

a. Are you currently a party to trackage rights agreements or arrangements If yes, how many and with whom?

Answer:

Yes. Burlington Northern is party to numerous trackage rights arrangements with other carriers involving relatively short distances of track. Most trackage rights arrangements are on the order of 40 miles or less, with a few exceeding 100 miles. The approximate current number of such arrangements is 5,618, not including short-term detour agreements. These arrangements involve about 65 other rail carriers including, among others, Soo Line; Chicago & North Western Transportation Company; Southern Pacific Transportation Company; Union Pacific Railroad Company; Chicago, Milwaukee, St. Paul & Pacific Railroad Company; Atchison, Topeka and Santa Fe Railway Company; Missouri Pacific Railroad Company; Conrail; MKT; Denver & Rio Grande Western; Family Lines; Illinois Central Gulf; and Kansas City Southern Railway Company. Burlington Northern has no trackage rights arrangements with non-railroad parties.

b. Does the industry have a standard form of trackage rights lease agreement?

Answer:

No. Each trackage rights arrangement is individually negotiated by the parties.

c. Is it your opinion that it would be unlawful for railroads to lease trackage rights to a shipper of coal, grain or other commodities? If you feel leasing of trackage rights would be unlawful, please cite the statutory provisions or legal precedents on which you rely for your conclusions.

Answer:

The concept of extending trackage rights to shippers raises major statutory and regulatory obstacles

and any statutory requirement mandating that such rights be made available to shippers would be an exceedingly unwise policy.

"Trackage rights" constitute a contractual arrangement between two or more railroads whereby, in a landlord-tenant relationship, the railroad tenant shares the landlord's common carrier facilities in order to perform common carrier service. They are voluntary agreements entered into for reasons of operating convenience, cost savings, or for other reasons involving mutual benefits. Such arrangements may be entered into by railroads only with prior approval of the Interstate Commerce Commission pursuant to 49 U.S.C. §11343, et seq. Approval is subject to a broad public interest standard. These are the only statutory provisions applicable to the implementation of trackage rights arrangements and do not address the possibility of shipper trackage rights. The ICC has no authority to force railroads to enter into §11343 transactions; its authority is strictly limited to approving or disapproving arrangements voluntarily proposed by carriers. St. Joe Paper Co. v. Atlantic Coast Line Railway Co., 347 U.S. 298 (1954). The ICC recently considered requests by coal shippers in Ex Parte 347 (Sub-No. 1), Coal Rate Guidelines--Nationwide to expand that proceeding to encompass the alternative of shipper trackage rights. In an unpublished decision served July 20, 1983, the ICC rejected that request on the grounds that only voluntary trackage rights arrangements between railroads are permitted by the Interstate Commerce Act, subject to ICC approval. Shippers are clearly not railroads and the concept of "shipper trackage rights" is just as clearly a misnomer. Shipper trackage rights, in contract to the historical meaning of the term, would involve the strictly private use of common carrier facilities for the exclusive benefit of a particular private non-railroad party and constitute a perversion of the term. Thus, there is considerable doubt that such an arrangement between a railroad and a shipper would be lawful under 49 U.S.C. §11343, et seq., and, clearly, there is no such mandatory statutory requirement with respect to railroads or anyone else.

Even if it were assumed for the sake of argument that a railroad-shipper "trackage rights" arrangement were not barred by 49 U.S.C. §11343, et seq., major statutory questions remain. If a shipper exercising such rights were considered a rail carrier

under 49 U.S.C. §10102(19) or a common carrier under 49 U.S.C. §10102(4), it would face major public interest hurdles before being permitted to operate and would be subject to numerous provisions under Title 49 governing its operations, which would effectively block its ability to function as a strictly private carrier for its own exclusive benefit, and violations of which would subject it to possible civil and criminal sanctions. See, e.g., 49 U.S.C. §11901, et seq. Moreover, under 49 U.S.C. §10746 it would be prohibited from hauling commodities which it wons or in which it has an interest. Again, assuming 49 U.S.C. §11343, et seq. would not bar such an arrangement, but viewing such a shipper-trackage rights tenant as a strictly private non-railroad and non-common carrier entity, other statutory obstacles arise which could subject the railroad and shipper both to severe criminal penalties. Such an arrangement could be viewed as an undue preference, interfering with a railroad's common carrier obligations, a rebate to a shipper, or discriminatory treatment of shippers, thereby violating several provisions of Title 49 and subjecting both parties to penalties under 49 U.S.C. §11901, et seq. See, also, Gallatin Coal & Coke Co. v. L&N RR CO., 55 I.C.C. 491 (1919); Ridge Coal Mining Co. v. M.P. RR CO., 62 I.C.C. 259 (1921); Second Industrial Railways Case, 34 I.C.C. 596. A railroad could not agree to extend trackage rights to a shipper without a significant risk that it would be required to do so for all other shippers under the existing statutory scheme and such arrangements would seriously undermine the common carrier concept on which Title 49 is based.

Major policy questions are also raised by the prospect of shipper trackage rights. The idea is being pursued out of a misplaced belief that the cost of private trackage rights operations would be less costly than otherwise applicable freight charges. This assumption has yet to be proven and any price which unfairly fails to adequately compensate the railroads would raise constitutional problems. Unfair financial arrangements would also fly in the face of the Staggers Act revenue adequacy goal. Furthermore, the only significant potential cost savings available to a shipper trackage rights operator (assuming it bears a fair share of maintenance and operations expenses and a fair rental) is in labor by displacing rail labor with private non-union employees of the shipper. "Shipper trackage rights" would also create an improper double standard for trackage rights

arrangements. Railroad trackage rights arrangements must meet a public interest test and by statute are subject to employee protective conditions. 49 U.S.C. §11347. Shippers seeking to enter into trackage rights arrangements seek to avoid that obligation. The concept also raises a fundamental policy question regarding the use of a national common carrier network for strictly private ends by parties having no public obligations and indeed seeking to avoid such responsibilities.

A final point should be made. Shippers seeking a right to obtain trackage rights are seeking a remedy unavailable to any other customer in any other industry. A purchaser of an automobile displeased with its cost does not have a statutory or common law remedy to obtain access to the manufacturer's plant in order to build his own car with his own labor. Yet, that is precisely the remedy shippers seeking trackage rights are demanding. And such an unheard of remedy is being sought notwithstanding the wide range of administrative and judicial remedies already available to shippers. Unless the Congress is prepared to totally reorder economic regulation in the United States, the concept should be discarded as the ill-conceived idea it is.

Question No. 2:

In testimony before the Judicial Committee on September 18, 1984, Thomas Stevenson, General Manager of Western Farmers Electric Cooperative, stated that in 1977 a quote of $11.94 per ton for shipping coal by rail had been offered by the Frisco railroad with the understanding that Burlington Northern supported the rate quote. This was before the Staggers Act took effect. Since then the two railroads have merged, Western Farmers now pays $23.69 per ton. Can you explain this exorbitant rate increase and offer statistical data to support your analysis?

Answer:

The difference between the planning rate furnished to Western Farmers in 1977 and our most recent quotation generally parallels railroad cost increases over the period. In October of 1977 we furnished a planning quotation of $11.94 per ton, subject to escalation by the AAR index, for coal to be delivered to the utility's plant at Ft. Towson, OK. This was three and one-half years before the movements actually started. Our most recent offer to Western Farmers is a rate of $21.96 per

ton subject to a 1.6 million ton annual minimum. On lesser volume, the rate would be $22.75. These two rates represent an increase over the $11.94 estimate of 83.9% and 90.5%, respectively. Over the same period, rail costs measured by the AAR indices increased 83.5% overall. Most of the increases in rail costs and commensurate rate increases occurred in the 1978-1980 period when diesel fuel costs more than doubled.

Question No. 3:

Many captive coal shippers are paying rates that are 200-300 percent higher than the railroad's cost of service. What is left to the shippers if both competition and regulation are ruled out? Isn't is inappropriate to term the rate setting procedure as "negotiations" if one party to the process controls the process?

Answer:

None of our unit train coal rates even approach the levels cited in this question. Competition between railroads, between modes of transportation and between coal producing regions is a significant influence on our pricing activities, it limits the rates we charge. Moreover, regulation is not ruled out. If we raised our rates to the levels specified in the question, if we did not lose the business--the most probable outcome--we would almost certainly face a challenge in the ICC.

Question No. 4:

On the average, how much have your rates on coal risen since 1976? How much on grain and fertilizer? How much on chemicals? Please be specific and support your figures with available data.

Answer:

Since 1976, rates (as measured by average revenues per ton mile) increased 9.5% per year for coal, decreased 3.3% per year for grain,[1] increased 4.9% per year for fertilizer and 6.6% per year for chemicals.

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[1] This figure includes processed grain and oilseelds, which constitute a small part of the total.

Question No. 5:

What is the average revenue-to-cost ratio that your company needs to earn to become "revenue adequate" according to the ICC? What is the average ratio on your coal traffic? Your grain and fertilizer traffic? Your chemical traffic? If you are not revenue adequate according to the ICC standards, where did Burlington Northern acquire the $700 million need to purchase El Paso Company?

Answer:

Revenue-to-cost ratio information is sensitive proprietary data which we prefer not to make public because knowledge of a company's costs in any industry provides its competitors with a singular advantage.

Burlington Northern has produced cash resources from sources other than railroad revenues. Among them have been the sales of Burlington Northern Air Freight Inc., the sale of one-half interest in the railroad company's Powder River Basin coal line to the Chicago and North Western railroad, and the one-time depreciation of track and roadway permitted by ERTA.

A point often overlooked in questions such as this, is that the railroad business is a cyclical one. During the upward swing of the business cycle, while huge investments must be made in railroad fixed plant and rolling stock (in the case of BN these investments have been at a historically high level), a revenue adequacy formula should permit a company to earn reserves for the inevitable down turn. Prudent investment of those reserves in a non-cyclical business, can insure the financial stability of the railroad during the time of reduced traffic and thinner margins. The El Paso Natural Gas acquisition fulfilled those objectives.

QUESTIONS SUBMITTED BY SENATOR BAUCUS

Question No. 1:

During a 1982 Judicial Committee hearing the Chairman and CEO of Burlington Northern, Inc., Mr. Richard M. Bressler, quoted me as saying: "We must all be prepared to acknowledge that Burlington Northern is entitled to make a reasonable profit. But we must be just as ready to assert that BN has a substantial obligation to serve the public as well." Mr. Bressler agreed with my assessment. Since the BN merger and the formation of your holding company, your profits have improved substantially, have they not? Would the BN now be willing to look at the other side of the coin--to recognize that reasonable freight rates are in the public interest?

Answer:

Burlington Northern's profits have improved owing to a multiplicity of factors: cost reductions, improved productivity, the general recovery of the economy, to mention some of the more important ones.

The second question presumes that profitability has come at the expense of Burlington Northern shippers. That presumption is at odds with the facts. Our two major commodities in Montana--coal and grain--make the point. Eighty-two percent (82%) of Montana coal, shipped on BN, moves under contract rates. That means that in 82% of our coal business, the shipper negotiated and agreed to a price that he found reasonable. Our answer to your third question shows clearly that in real terms our grain rates have declined compared to 1980 rates.

The second question also presumes that we do not consider the effects of our transportation charges on our customers. The organization of our Marketing Department into business units, which match the special needs of our various shippers, is but one of the changes we've made to form a partnership with our customers. The growing number of contracts and the expansion of our shares in many of our markets suggest that our customers find that our rates and service indeed are reasonable.

Question No. 2:

Could you tell me what the current rates for a 26-car and 52-car train now are between Omaha, Nebraska, and Portland, Oregon? Also, what are the rates from Wolf Point, Montana, to Portland, Oregon?

Answer:

The rates on wheat from Omaha, Nebraska, and Wolf Point, Montana, to Pacific Northwest Ports are as follows for 26- and 52-car shipments:

(Rates in cents per 100 pounds, from BN Tariff 4022-D)

	26-Cars	52-Cars
Omaha, NE	195¢	180¢
Wolf Point, MT	176¢	161¢

Question No. 3:

I have been told by the Burlington Northern in the past that unit train rates from Nebraska to the West Coast are lower than from Montana to the West Coast. Is this because the BN faces competition in Nebraska and in Montana there is no competition?

Answer:

The rates on wheat from stations in the State of Montana and from stations in the State of Nebraska are lower from the western stations in each state than they are from the eastern stations in each state. And as seen in the answer to question number 2, some Nebraska rates are higher than Montana rates, but, some Nebraska rates are lower than some Montana rates.

Burlington Northern faces competition in all of the states where we originate grain. In Nebraska, we face truck competition, and must compete with other railroads both for traffic to terminals such as Kansas City, MO-KS, as well as export traffic to Gulf Ports and West Coast Ports. From Montana, we are faced with competition from the Union Pacific in the Butte area and from the Soo Line Railroad in the northeast corner. More importantly, however, we face competition across the State of Montana from trucks hauling grain in backhaul service to the Coast and to transfer points on the Columbia and Snake River systems for movement by barge to Columbia River export houses. In fact, during the six-month period of June to December 1980, trucks handled nearly 51% of the wheat shipped out of Montana. During this period the Staggers Act became law, and we established reduced single car and unit train rates on wheat from Montana. Since that time, we have been able to increase rail share of Montana's wheat shipments by means of more efficient operations and consequently lowered costs, enabling BN to better meet its competition.

Attached is a graph containing a comparison of Montana's rates on wheat to Pacific Northwest Ports for the period 1970-1984. This graph was not prepared by BN, but rather a traffic consulting firm, Radermacher and Associates, and it does accurately show the rate structure through the time period in question. The graph and the description of Montana's wheat rates and the effect of competition are typical of grain rates throughout BN's system.

On December 1, 1980, BN established its unit train structure from Montana, Wyoming, and the western third of North Dakota to the Pacific Northwest to recapture traffic being lost to truck-barge over Lewiston, Idaho, and other Snake River barge terminals. Single car rates were reduced by 15 cents; another 15 cents was taken off for 26-car two to four location rates; another 5 cents was taken off for 26-car single location rates; and still another 5 cents was taken off for 52-car single location rates.

On February 28, 1981, single and 26-car rates were established from various Montana origins to Spokane, WA, at rates lower than established earlier to coast destinations. These adjustments were necessary to meet truck competition.

On December 1, 1981, some minor reductions were made in the Pacific Northwest and Spokane structures to further meet motor carrier competition.

On April 19, 1982, the Pacific Northwest rates were regraded for truck-barge competitive reasons.

On July 1, 1982, we added 52-car rates to the Spokane rate structure in an effort to achieve further economies of scale thereby lowering costs and enabling lower rates to meet highway competition.

On July 20, 1982, we reduced our rates from the northeast corner of Montana to the Pacific Northwest to meet action taken by other rail carriage. Soo Line rates in connection with Canadian Pacific and Union Pacific were reduced making further competitive reductions on the BN necessary.

Effective August 8, 1983, we reduced the 26- and 52-car single location rates by 5 cents from Glasgow and West and from Mocassin and Lewistown north. This was necessary to meet further truck-barge competition.

These structures were originally established in December of 1980, but because of competition, we did not receive the full benefit of Rail Carrier Cost Recovery increases

that have been authorized to apply on this traffic. The increases authorized are as follows:

Date	
12-30-80	Ex Parte 386 authorized 5% increase.
1-17-81	Ex Parte 311-c (later incorporated into RCCR 001) authorized a 1.1% surcharge.
2-20-81	Ex Parte 311-D (later incorporated into RCCR 001) authorized an additional surcharge of 1.1%.
4-07-81	Ex Parte 311-E (later incorporated into RCCR 001) authorized additional surcharge of 0.7%.
6-05-81	RCCR authorized an increase of 1.1% and incorporated the surcharges from X-311-Series for a total of 4% (later incorporated into RCCR 003).
7-01-81	RCCR 002 authorized an increase of 2.8% (later incorporated into RCCR 003).
10-01-81	RCCR 003 authorized an increase of 1.4% and incorporated increases from RCCR 001 and RCCR 002 for total of 8.4%.
1-01-82	RCCR 082 authorized an increase of 4.7%.
1-01-83	RCCR 083 authorized an increase of 1%.
10-09-83	RCCR 083-A authorized 0.2% increase to be incorporated with RCCR 083 for total of 1.2%.
1-01-84	RCCR 084 authorized 4.1% increase.
7-01-84	RCCR 084-A authorized additional 0.4% increase when incorporated with RCCR 084 totals 4.5%.

As can be seen from the following rate comparison, the cost-based increases were authorized but the market place would not allow increased rates if we were going to hold this traffic to rail. It should also be pointed out that the following comparison draws the rates from points in Eastern Montana closer to those applying from the Great Falls-Havre-Cut Bank (so-called Triangle) area. From the nine origins shown as examples, four currently have rates lower than December 1, 1980. Four

have rates only slightly higher than December 1, 1980, and one has exactly the same 52-car rates as when the unit train program was established, December 1, 1980.

Origin	52-Car Rates as of 12/1/80	If All Increases Had Been Added	Present	Differences in Rates vs. Great Falls		
				12/1/80	If All Increases Applied	Today
Billings	140¢	176¢	129¢	29¢	36¢	13¢
Bozeman	115	145	120	4	4	4
Glendive	170	214	169	59	76	53
Great Falls	111	141	116	-	-	-
Havre	126	159	126	15	19	10
Kalispell	99	124	98	Lower	Lower	Lower
Miles City	165	208	154	54	68	38
Plentywood	168	211	169	57	71	53
Wolf Point	159	201	161	48	61	45

RESULT OF RATE ACTIVITY

Our activities have increased our market share of both total wheat moved out of Montana and specifically wheat destined to coast points only because we offer the best transportation package--not because we're the only carrier. Unit train shipments have made it possible for greater wheat shipment from Montana than could otherwise have been made. Total shipments and rail handling have grown quite large without the chronic car shortages that existed in the late 1970's.

We know that unit train shipments, specifically 52-car shipments, now have a major share of the market place due to cost effective rates and services. We also now realize that 52-car shipments are the basis for trading wheat on West Coast exports. For example, on October 12, 1984, the cash price offered at Great Falls for 11% protein, hard red winter wheat was $3.47 per bushel. At Portland, the first half October delivered price was $4.22 per bushel (it has been $4.24). The difference between $4.22 at Portland and $3.47 at Great Falls is 75¢ per bushel or $1.25 per cwt. The Great Falls 52-car rate is $1.16 per cwt., leaving 9¢ for handling, elevation, etc. Thus making it clear that the most efficient form of transportation, i.e., 52-car shipments, set the price for Montana's wheat.

Most important, however, is the improvement in price received by the producer, which we can estimate.

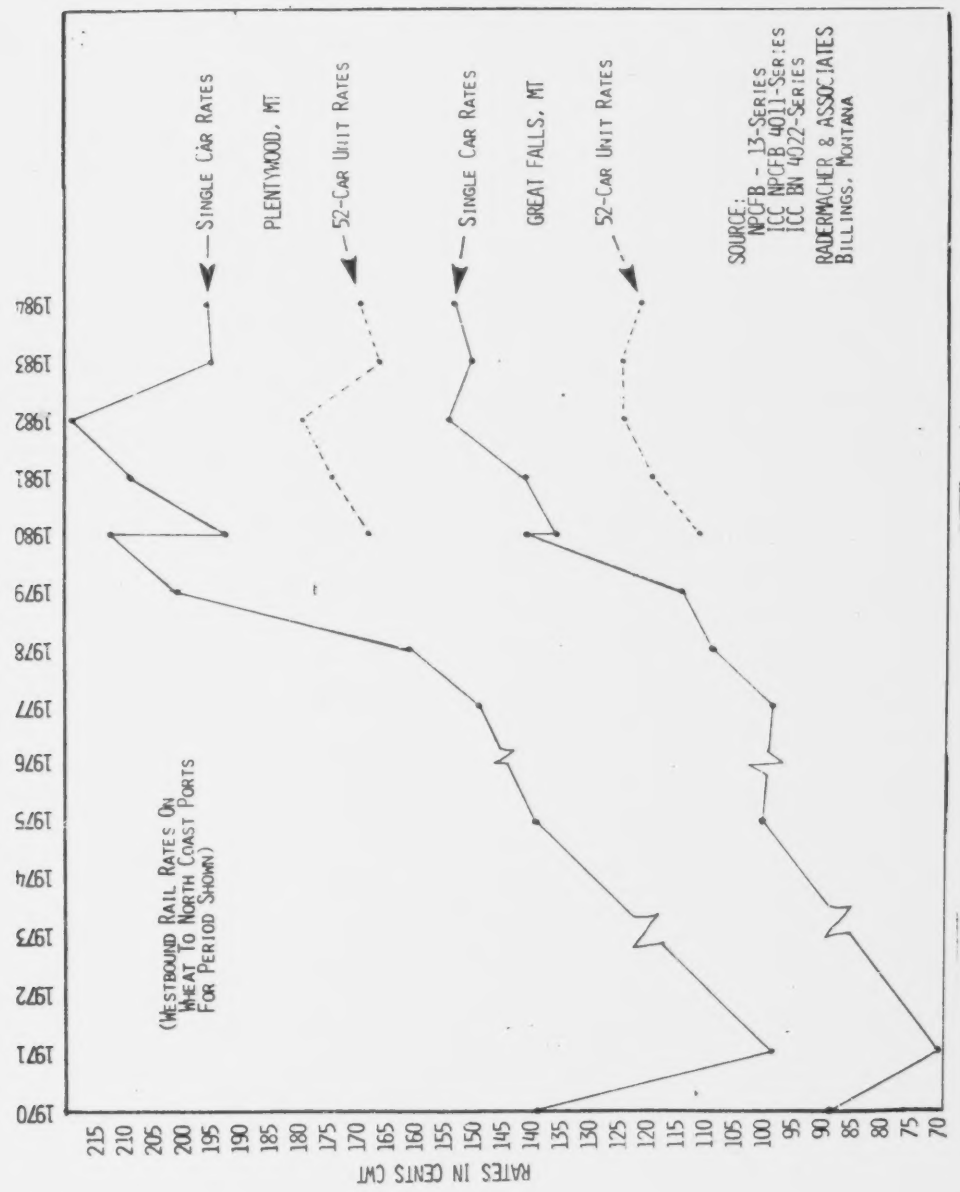
Historically, before unit trains, the single car basis would factor into the origin vs. destination pricing of grain. Today's single car rate from Great Falls is 153¢ per cwt. This converts to 22¢ per bushel. If we are now handling over 95 million bushels of Montana wheat westbound by rail, and if the 52-car basis is used for grain pricing, then $20 million dollars are now passed on to producers in the form of higher grain prices due to our unit train program. That's $20 million dollars every year that are left in the State of Montana for other purposes.

Question No. 4:

I have a letter here from Mr. Richard Riley, Sales Manager for F. G. Stoltze Land and Lumber Company in Columbia Falls, Montana. I want to ask that a copy of the letter be included in the hearing record. Mr. Riley is in the lumber business and relies totally on Burlington Northern to ship his products. Mr. Riley has lost business because he is charged higher freight rates than his competitors in the northwest. Would you be willing to supply an answer to Mr. Riley's letter for the record?

Answer:

We were pleased to respond to that letter in a reply to you on October 18. A copy is attached for the hearing record.


(Westbound Rail Rates On Wheat To North Coast Ports For Period Shown)
Single Car Rates
Plentywood, MT
52-Car Unit Rates
Single Car Rates
Great Falls, MT
52-Car Unit Rates
Source:
NPCFB - 13-Series
ICC NPCFB 4011-Series
ICC BN 4022-Series
Rademacher & Associates
Billings, Montana
Rates in Cents CWT
1970
1971
1972
1973
1974
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1976
1977
1978
1979
1980
1981
1982
1983
1984
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BURLINGTON NORTHERN RAILROAD

LAW AND
GOVERNMENT AFFAIRS

3800 Continental Plaza
777 Main Street
Ft. Worth, Texas 76102

817-878-2364

October 18, 1984

Honorable Max Baucus
706 Hart Building
Washington, D. C. 20510

Dear Senator Baucus:

Your inquiry on behalf of Mr. Richard D. Riley of the F. H. Stoltze Land and Lumber Co. was forwarded to me by our Washington, D. C. office.

The contract provision of the Staggers Act is one of its most popular innovations according to our shippers. It has given us the pricing and service flexibility that other businesses have long enjoyed. Among other mutual advantages, we can tailor rates and service to the volume capability of our customers. The derivative benefits of this new mode of business are closer, more frequent communication with the shipper, better service and lower rates, and productivity improvements owing to more predictable volume movements.

In tailoring a contract we have special concern for the competitive environment of our customers. We try to recognize the benefit due a shipper who can ship in volume, while at the same time avoiding the possibility of putting a smaller competitor at a serious disadvantage.

We and our customers are prohibited from revealing the terms of our contracts. But a contract just about always offers the shipper more favorable terms than the published tariff rate. In that connection, we have held those tariff rates to approximately the levels that existed in July, 1981, to help our customers through this difficult period. Consequently, contract benefits are in addition to a stable rate base which, in real dollar terms, is lower than it was three years ago.

Another factor keeps a downward pressure on our rates (in addition to our desire to keep the delivered price of Montana forest products competitive). That is the pervasiveness of motor carriers. Trucks claim a substantial portion of the transportation market for forest products in Montana, and we are in day-to-day, head-to-head competition with them.

I would conclude by stressing a point made above: The Staggers Act, as a collateral benefit, put us much closer to our shippers than ever before. We like to think of ourselves as partners with them. In that spirit, I hope we can continue to work with Mr. Riley, and discuss -- within the constraints of the law -- ways to satisfy his concern.

Very truly yours,

Ronald H. Reimann

RHR:pt

Senator DECONCINI. Mr. Donahue, thank you. I wish I could stay here to ask some questions because your statement provokes many disputes in my mind. I do have questions here that I would like to ask both of you to consider answering from Senator Baucus, and I would submit some, also, that I would appreciate your answers to.

We do have two additional statements here from Ronald G. Wasson and Reese H. Taylor which we will insert in the record at this point.

[The following were received for the record:]

STATEMENT OF RONALD G. WASSON
VICE PRESIDENT OF PURCHASING
KANSAS CITY POWER & LIGHT COMPANY

BEFORE THE SENATE CONSTITUTION SUBCOMMITTEE
September 18, 1984

I am Ronald G. Wasson, Vice President of Purchasing, Kansas City Power & Light Company. The company provides electricity to some 345,000 customers who reside in 94 incorporated communities in 23 western Missouri and eastern Kansas counties.

I am presenting my views, and the company's, on S.2417 regarding railroad trackage rights and their usefulness in protecting consumers from the railroad exercise of monopoly power. Our customers have a vital stake in this legislation, since it holds a key to keeping down the rates they pay for electricity.

Let me provide you with a real life example of the trackage rights issue. Iatan Station, located some 45 miles northwest of Kansas City, is a 670 MW coal-fired unit jointly owned by Kansas City Power & Light Company, St. Joseph Light & Power and Empire District Electric Company. This plant was designed to burn low-sulfur western coal and requires about 2.5 million tons of coal per year. The annual fuel cost for the plant is about $51 million of which $35.6 million, or 70 percent, is transportation cost. The plant is presently served by the Burlington Northern Railroad delivering coal in unit trains owned by KCPL from the Powder River Basin area near Gillette, Wyoming. Burlington Northern is the only rail carrier presently having access to this plant; consequently, they hold a monopoly on coal shipments to Iatan.

We have recently requested bids from Burlington Northern and their competitors for transportation from the Powder River Basin to Iatan. The specific results of that

bidding process are of necessity confidential, since we have not yet awarded this business; but the case for trackage rights is strongly supported by our evaluation of the bid offers. Our evaluations reveal that trackage rights could save about $40 million on a net present value basis over the 20 year life of a transportation agreement at Iatan by simply allowing the competing rail carrier to deliver coal to the station at a reasonable fee for the use of Burlington Northern's tracks. The alternative to trackage rights is physical construction of connecting rail lines to the competing railroad, either through a new state park which is currently under development or across a railroad bridge which must be constructed spanning the Missouri River. The construction costs of these alternatives ranges up to $40 million under certain scenarios.

The distance from the Powder River Basin area to the plant is about 800 miles, and while the competing carrier comes within about 6 miles of the plant, access over existing rail facilities is not readily available. It would seem only reasonable that a carrier who can deliver the coal for 99+ percent of the distance should be allowed to compete, and our customers should be afforded the economic benefits of such competition; but today's rules do not provide a means of access which promotes effective rail competition.

Trackage rights represent an ideal solution in this instance, because they would eliminate the monopoly enjoyed by the Burlington Northern, our customers would enjoy the resultant savings in fuel costs and they represent the most economically efficient solution, since construction of duplicative rail facilities would be avoided.

In summary, Kansas City Power & Light Company strongly favors the granting of railroad trackage rights in instances where they provide an effective remedy to railroad monopoly power.

STATEMENT OF REESE H. TAYLOR, JR., CHAIRMAN
INTERSTATE COMMERCE COMMISSION
BEFORE THE SENATE COMMITTEE ON
THE JUDICIARY ON S. 2417

September 18, 1984

Mr. Chairman and Members of the Subcommittee:

I want to thank you for this opportunity to submit the views of the Commission on S. 2417, a bill to "amend the Sherman Act to prohibit a rail carrier from denying to shippers of certain commodities, with intent to monopolize, use of its track which affords the sole access by rail to such shippers to reach the track of a competing railroad or the destination of shipment."

The stated purpose of the bill is to insure a greater measure of competition in the rail industry for shipments of coal, ore, grain, forest products, chemicals, or fertilizers. It seeks to enhance competition in areas now served by only one railroad in an effort to insure the benefits of competitive prices to consumers and the shippers that serve them.

S. 2417 seeks to accomplish this goal by making it unlawful for a rail carrier, with intent to monopolize, to deny to any shipper of the above-listed commodities the use, on reasonable terms, of a railroad facility which is the sole facility providing rail services to that shipper. An "intent to monopolize" is conclusively presumed if the carrier: (1) has

denied use of the railroad facility[1] upon reasonable terms to a shipper; and (2) is not permitting any other carrier to use the railroad facility to serve the shipper. Finally, the bill provides that the terms offered by the rail carrier shall not be deemed reasonable if: (1) they condition the use of the sole facility upon use of other facilities of the rail carrier; (2) the rates required by the rail carrier for use of the sole facility are such as to yield a revenue-to-variable cost ratio higher than the lower of the revenue-to-variable cost ratios yielded by - (i) its single line rate or (ii) its division of a competing joint line rate; if there are such, to the destination of shipment; or (3) the rates required by the rail carrier for use of the sole facility are higher than would, under generally accepted regulatory standards, yield a fair return on the proportion of the rail carrier's prudent investment in the railroad facility that the shipper's traffic bears to all traffic using such railroad facility. The bill does not specify who is to make these determinations. While the Staggers Act accords the railroads substantial rate freedom, we would note that, to the extent rates remain subject to review, the Commission has exclusive jurisdiction to determine the reasonableness of rates and charges of rail carriers subject to ICC jurisdiction.

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[1]Defined to include all railroad components enumerated in 49 U.S.C. §10102(20), namely--

(A) a bridge, car float, lighter, and ferry used by or in connection with a railroad;

(B) the road used by a rail carrier and owned by it or operated under an agreement; and

(C) a switch, spur, track, terminal, terminal facility, and a freight depot, yard, and ground, used or necessary for transportation.

In essence, S. 2417 attempts to restrain rail rates for shippers using rail service by requiring a rail carrier to allow trackage rights over its lines to another carrier in order to permit that carrier access to the shipper. If the origin carrier denies use of the facility on "reasonable" terms to such a shipper and also refuses to allow access over its lines to the shipper by another carrier, the origin carrier would be conclusively presumed to have acted unlawfully with intent to monopolize.

The Staggers Act was intended to assist the rail system to remain viable in the private sector and to allow the railroads to compete more effectively among themselves and with other modes of transportation. While there is greater reliance on the forces of the marketplace, a regulatory process remains to balance the needs of carriers, shippers and the public where warranted, such as in the absence of effective competition.

We believe, and have so testified before the Senate Commerce Committee and the House Committee on Energy and Commerce, that, in general, the Staggers Rail Act is working well. In our view, the Act and our implementation of it have been successful in removing unnecessary regulation, encouraging efficient carriers to earn adequate revenues, and balancing the interests of the parties in accordance with the goals of the Act. Many of the provisions of the Staggers Act, such as the provision authorizing and encouraging the use of contracts and the provision restricting rate bureau activities, have resulted in more effective competition among rail carriers and with other modes. We recognize,

however, that certain changes in railroad policy and operations have been unpopular. Once of those changes has been in the area of reciprocal switching, one method of alternative access. The Staggers Act prompted rail carriers to review existing arrangements and to limit some of these arrangements to reflect existing competitive conditions and revenue need.[2]

It is this area of concern to which S. 2417 is directed. But S. 2417 would go further and, given the possibility of Sherman Act prosecution, would have the effect of requiring trackage rights on any part of a carrier's system rather than being limited as is §11103 to reciprocal switching arrangements in terminal areas. As a result, this bill presents a number of practical problems. We are also concerned that it does not reflect the basic economic policies of the Staggers Act and the balance that was intended in that Act.

The bill fails to consider legitimate operational concerns. 49 U.S.C. 11103 recognizes that alternative access must be "practicable" and must not impair the primary carrier's use of its facilities. This is a complex question of fact. Authorizing access should not be permitted to cause inefficient operations by either or both carriers. The bill further complicates matters by authorizing shipper operation of rail equipment. There are also implications for labor (if traffic is diverted) and questions of liability for accident or misuse by shippers.

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[2] See the discussion in the attached Ex Parte No. 445, Standards for Intramodal Rail Competition, served July 7, 1983, at pps. 9-11.

We also note there is no limit to the distance for which trackage rights would in theory be available for coal, ore, grain, forest products, chemicals or fertilizers. If this is not addressed, the bill could have the effect of creating a nationalized trackage system for these commodities and artificially control prices for track rental.

Finally, the bill would not allow consideration of competitive circumstances in determining whether access should be granted or determining the price for the rail service. The bill's definition of "reasonable terms" does not allow any consideration of demand elasticity, differential pricing, or revenue need. Rail carriers must be permitted to price services efficiently and with reference to the particular situation if they are to be profitable in the private sector. The bill prohibits them from doing so for the above-listed commodities, and instead establishes an artificial rate standard bearing no relation either to the individual movement or to the carrier's overall revenue need.[3]

We hope these comments point out the complex questions that must be answered before rail carriers are required to allow competitors to operate over their lines (or risk Sherman Act prosecution). We are concerned that S. 2417 fails to take account of these matters. As far as terminal-related access, we believe present §11103 is a preferable vehicle and we have used it to authorize alternate service where appropriate and necessary

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[3] Section 9(a)(2)(C) also establishes the extremely complex task of determining what a railroad's "prudent investment" is. More specific guidelines would certainly be needed to minimize litigation in this area.

to competition and in the public interest.[4] Trackage rights on any part of a carrier's system is far broader and with great potential impact. It is an idea that we believe needs considerably more study prior to any action being taken.

CHAIRMAN TAYLOR, concurring:

I would point out that the Commission is mindful of the need to keep fully informed as to the impact of the Staggers Act on both carriers and shippers. To that end, we recently implemented a new proceeding, Ex Parte No. 456, to (1) gather and analyze information from rail carriers and shippers concerning the implementation and effect of recent rail legislation, particularly the Staggers Act; and (2) offer a forum for direct discussion of problem areas by those directly affected.

This proceeding's structure and direction will be guided by the Commission's Chief Administrative Law Judge. Common interest conference groups may be formed, under the Chief Administrative Law Judge's supervision, in key areas such as contracting, reciprocal switching, revenue adequacy, market dominance criteria, maximum reasonable rate guidelines, joint rate and route cancellations, etc. The information obtained will assist us in evaluating our implementation of the Staggers Act. The proceeding will also provide a forum for carriers and shippers to meet and may lead to a greater consensus among all parties as to

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[4] See Ex Parte No. 445, supra, footnote 15, and Delaware & H. Ry. Co. v. Consolidated Rail Corp. 367 I.C.C. 718 (1983), attached. The latter case demonstrates how complex this area is and the countervailing interests that must be balanced.

the proper role of regulation in today's rail transportation markets. Additionally, the proceeding will offer opportunities for resolving commercial disputes without recourse to agency, court, or legislative intervention.

We will keep you informed as Ex Parte No. 456 progresses. It should provide information which may be of assistance in connection with the problems S. 2417 seeks to address. Additionally, the proceeding could alleviate some of the problems cited as justification for the proposed legislation.

EC
FR-7035-01

INTERSTATE COMMERCE COMMISSION

DECISION

SERVICE DATE

Ex Parte No. 445

JUL 7 1983

STANDARDS FOR INTRAMODAL RAIL COMPETITION

AGENCY: Interstate Commerce Commission.

ACTION: Denial of Petition for Rulemaking.

SUMMARY: This decision denies the petition to begin a rulemaking proceeding relating to rail rate changes, route restrictions, and terminal operations. The Commission is, however, undertaking an in-depth study of the changes that are occurring, their reasons and their effects, and will use the results of that study to determine whether further action is necessary. If necessary in conjunction with the study, we may request comments in specific areas at a later date.

FOR FURTHER INFORMATION CONTACT: Louis Gitomer (202) 275-7245

SUPPLEMENTARY INFORMATION:

In a petition filed February 25, 1983, the National Industrial Transportation League (NITL) requested the Commission to institute a rulemaking proceeding[1]/ for the purpose of issuing rules to:

(1) prohibit anticompetitive railroad cancellations of joint rates and through routes, and the closing of gateways; and

(2) implement the pro-competitive provisions of the Staggers Rail Act of 1980 (Staggers Act)[2]/ pertaining to reciprocal switching arrangements and joint use of terminal facilities, through trackage rights or otherwise.

NITL expresses strong concern for recent developments in the area of railroad cancellations of rates, routes, gateways, reciprocal switching arrangements and arrangements for joint use of terminal facilties.[3]/ It argues that many of these

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1/ In a second petition filed March 4, 1983, NITL requests (1) immediate institution of the rulemaking proceeding proposed in its earlier petition; and (2) postponement of the March 14, 1983 effective date of certain rail tariff supplements until completion of the proposed proceeding. Those tariff supplements were protested, and the Commission's Suspension Board, in Suspension Case No. 71026) declined to suspend or investigate; thus, the provisions became effective as scheduled. An appeal of the Board's decision was denied by Division 2 on March 11, 1983. NITL filed a petition seeking expedited consideration on April 29, 1983.

2/ Pub. L. No. 96-448, 94 Stat. 1895.

3/ NITL indicates that the Commission is in a position to take official notice of the phenomenon of increasing cancellations of railroad routes and rates. In appendices B and C of its petition, NITL submits excerpts from the Journal of Commerce (February 16 and 17, 1983) to illustrate the magnitude of the problems involved in recent cancellations.

cancellations, which are nationwide in scope, are anticompetitive, contrary to the public interest, and ultimately will undermine the unified, national rail transportation network.

In support of its position, NITL submits that a fundamental objective of the Staggers Act was to encourage and promote carrier competition, including intramodal rail competition and points out a number of pro-competitive goals of the national rail transportation policy at 49 U.S.C. 10101a.

NITL asserts that widespread cancellations impose an overwhelming burden on the shipping public and are incompatible with the Staggers Act and the rail transportation policy. Further, it suggests that such actions, when taken by carrier conglomerates, may pose antitrust problems under 15 U.S.C. §1, et seq.

In addition to requesting a rule to prohibit "anticompetitive" cancellation of reciprocal switching agreements, NITL seeks the issuance of a related rule "manadating the encouragement and implementation" of both reciprocal switching agreements and arrangements for joint use of terminal facilities in order to provide for the needs of the shipping public and to promote railroad competition in accordance with section 223 of the Staggers Act [49 U.S.C. 11103(c)]. NITL neither defines terms such as "anticompetitive" and "mandating... encouragement," nor proposes rules to accomplish these goals.

Section 223(c) authorizes the Commission to order reciprocal switching wherever "it finds such agreements to be practical and in the public interest, or where such agreements are necessary to provide competitive rail service." NITL asserts that section 223(c) contemplated not only the retention but the expansion of reciprocal switching arrangements. NITL further contends that the rail transportation policy dictates vigorous implementation of the provisions for joint use of terminal facilities stated in 49 U.S.C. 11103(a).

To avoid the burden, delay, and expense of individual litigation on a case-by-case basis, NITL maintains that rulemaking, rather than adjudication, is administratively efficient and appropriate to establish standards which will determine when a cancellation of route and rate, or a termination

of reciprocal switching agreement, or termination of an arrangement for joint use of terminal facilities is anticompetitive in nature.

Statements supporting the petition were filed by various shippers (see Appendix). Shippers generally argue that the large number of cancellations of through routes,[4] joint rates, and reciprocal switching arrangements violates the spirit and intent of the Staggers Act, which is to promote intramodal rail competition while reducing government regulation of the railroads. They assert that these cancellations eliminate shippers' transportation alternatives, cause shippers to use circuitous, less efficient routes and thereby incur additional transportation costs, and impair the shippers' ability to enter into transportation contracts with certain carriers. Shippers further argue that this prevents them from using the most efficient rail transportation routes, requires substantial changes in distribution methods, and also may create safety problems if they are required to use motor carriage for the transportation of hazardous materials. They project that the continued trend toward cancellations and similar restrictive tariff actions will result in the virtual absence of intramodal competition.

Consolidated Rail Corporation,[5] Soo Line Railroad Company, and the Chicago, Milwaukee St. Paul and Pacific Railroad Company, Debtor (Richard B. Ogilvie, Trustee) (Milwaukee Road), also support the petition. Soo Line expressed concern that its ability to enter into allowance contracts has been jeopardized by restrictive tariff amendments designed to limit the applicability of existing rates to the canceling carrier's long haul. Milwaukee Road contends that recent railroad cancellations and similar restrictive tariff actions have adversely affected all of

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[4] We are unaware of carrier actions allowed to become effective that physically close routes. Rate actions that restrict rates over particular routes do not close them, per se.

[5] Although Conrail supports the petition for rulemaking, it believes that an investigation will result in a determination that no rules should be adopted. It would require NITL to submit more specific information as to possible new rules.

its gateways, numerous commodities, some of its basic operational patterns, and its ability to achieve revenue adequacy and to utilize transportation contracts. It emphasizes that these cancellations essentially are filed by large carriers with the objective of preserving the route and rate that accords the canceling carrier its longest haul. As a regional carrier, Milwaukee Road insists that it is vital that it be permitted to compete with other railroads through all of its gateways.

Replies in opposition to the petition were filed by the Burlington Northern Railroad Company (BN) and Illinois Central Gulf Railroad Company (ICG). Essentially, they argue that the Interstate Commerce Act, as amended, clearly establishes the principles under which route and rate cancellations, reciprocal switching arrangements, trackage rights and other operations and services are to be considered. Thus, they view the proposed rulemaking as essentially restating the statutory criteria and serving no useful purpose.

BN and ICG point out that the current statutory and regulatory scheme under which the Commission, the railroads, and the shipping public must function is marked by clear Congressional directives to reduce regulation, and to permit the marketplace to determine, to the maximum extent possible, the nature and price of railroad services. They submit that the issues raised by NITL are best addressed in a case-by-case analysis, as only by individual adjudication, can efficiency, revenue, redundancy, energy, and competitive issues be accorded adequate and factual consideration.

While the breadth of the actions taken raises legitimate concerns, we remain supportive of the direction of these changes. Accordingly, we will address the key issues here. In order to respond to the NITL petition it is initially necessary to review recent actions relating to joint rate and reciprocal switching cancellations and some of the bases for those actions.

Background

A. Legislative Actions. In October of 1980, the Staggers Rail Act of 1980 became law. This represented the second major

effort in five years[6] to resolve the continuing problem of railroad revenue adequacy. The legislative history states, in part.

> Earnings by the railroad industry are the lowest of any transportation mode and are insufficient to generate funds for necessary capital improvements. By 1985, the railroad industry will experience a capital shortfall of between $16 billion and $20 billion . . . . Modernization of economic regulation of railroads, with greater reliance on the market place is essential to achieve maximum utilization of railroads, to save energy and to combat inflation. H.R. Rep. No. 96-1430, 96th Cong. 2nd Sess. 79 (1980).

Congress enacted a new rail transportation policy, made findings and set goals, all of which emphasize the need for railroads to earn adequate revenues. The statute reflects a legislative intent "to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates." 49 U.S.C. 10101a(1). See also 49 U.S.C. 10701a(b)(3). The regulatory scheme was substantially reformed in order to free rail rates from regulation in all but those limited instances where effective competition does not exist. H.R. Rep. No. 96-1430, supra, at 89.

Congress also spoke extensively to the issue of revenue adequacy in the joint rate context. It noted:

> Two of the major problems caused by the existing joint rate system are too low rate divisions and a proliferation of uneconomic routes protected by the archaic "commercial closing" doctrine.[7] Id. at 111. (emphasis supplied)

In response, Congress provided additional remedies for depressed earnings on joint movements.[8] However, it stated it had no intent to limit a carrier's existing rights to secure improved earnings over specific routes. It found that, beyond the new

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[6] The first was the Railroad Revitalization and Regulatory Reform Act of 1976 (the 4R Act).

[7] This doctrine, since abandoned, held that any rate increase to a joint movement making one route more expensive than another route between the same points, cancelled the joint route for purposes of invoking §10705(e) jurisdiction.

[8] See, e.g. 49 U.S.C. 10705a. While this provision has been used by a number of carriers, it is not the gravamen of the NITL petition, and activities under it will not be discussed in depth here.

extraordinary procedures, existing remedies [10705(e)] should be adequate "assuming the Commission chooses to administer them in order to realize the revenue adequacy goals of the Act." Congress recognized a serious problem with the existing joint rate structure and anticipated that revisions would be undertaken by rail carriers.

In another action that had a direct impact on carrier activities, Congress addressed the way in which railroads should price joint line service. See 49 U.S.C. 10706. In expanding the limitations on collective activity first enacted in the Railroad Revitalization and Regulatory Reform Act of 1976, Congress restricted joint line price discussions to require carriers to conduct separate meetings covering each particular route.

Realizing that these changes would, if taken advantage of, dramatically change both railroads' services and their pricing, Congress offered new protection in the form of an amendment to 49 U.S.C. 11103. This amendment expanded the Commission's discretion to require reciprocal switching where practicable and in the public interest, or where necessary to provide competitive rail service.

B. Administrative Actions. In direct response to the Staggers Act, the Commission took a number of actions that have affected railroad pricing of joint services.9/

9/ Actually, the impetus for much of the rail activity being challenged came before the Staggers Act. In fact, these statutory amendments addressed inadequacies in the prior statute. Serious joint line rate problems were exposed in a number of earlier Commission proceedings. In No. 37646 (Sub-No. 66) et al., Hog Hair, Versailles, Ohio to Etowah, Tenn., not printed, decided March 21, 1980, the Commission addressed an ongoing dispute between the Family Lines System and the Southern Railway Company concerning the question of rate equalization for competing single line and joint line routes. The Commission said there:

> "The fact that rate parity once existed between single and joint line routes does not mandate a finding of unlawfulness when that rate parity is changed by publication of new lower single line rates . . . . [P]rotestant has no right to participate as a connection in movements originated by other carriers."

Soon after, the Commission issued decisions in Conrail Surcharge on Pulpboard, 362 I.C.C. 740 and 843 (1980). In that pre-Staggers Act case the evidence clearly established that Conrail's division of joint rate revenue often did not cover its variable cost of service. The Commission discussed the need to review and identify routing that were unprofitable and suggested use of the cancellation remedy under 49 U.S.C. 10705(d) [now (e)].

In Western Railroads Agreement, 364 I.C.C. 635 (1981), the Commission undertook to implement limitations on collective ratemaking. In the past, all railroads that could participate in service between two points often decided upon, with antitrust immunity, a uniform rate between those two points regardless of routing.10/ The concerns of many that routing would become limited due to the new requirement that participants in particular routes price separately was discussed. The Commission concluded that:

> If this occurs, we can see no harm to the carriers or the shipping public in reducing the number of routes. We recognize that under the current route system, shippers have numerous options . . . . To the extent that our definition . . . will result in the loss of some routes . . . that effect is outweighed by the desirability of more efficient routing . . . . Those routes which remain in shipper demand and which are profitable . . . will continue . . . . The elimination of costly, circuitous and inefficient routes will benefit the industry as well as its customers . . . . Carriers are free to create rates for new traffic in which they would participate, and are encouraged to pursue aggressively potential shippers with competitive offers of service. pp. 649-650.

The Commission also noted that, should carriers act to restrict routing, there were remedies (under the statute and the antitrust laws) against cancellation of joint rates and routes. See e.g., §10705(e). The Commission may also prescribe joint rates under certain circumstances. See §10705(a). The decision acknowledged that some bridge (intermediate) carriers might lose business which they had under the prior open routing system. However, the Commission found that this outcome was contemplated by the Staggers Act.

In March of 1982, the Commission took another important action to implement the Staggers Act's policy of greater flexibility in the joint rate structure. Since the 1920's, the Commission had imposed so-called DT&I conditions intending to lessen the impact of rail consolidations on nonapplicant

10/ Obviously, this "open routing" was not market or cost-based pricing. For example, the shipper would pay the same amount whether the route chosen was 1,000 or 2,000 miles and whether there were one, three, or more carriers involved.

railroads and the public. As pertinent here, Condition 1 had been interpreted to require rate equalization between a new single line routing (created by the merger) and competing joint line routes in which the consolidated carrier participated. The other conditions imposed similar strictures, generally preventing the consolidated carrier from preferring its own lines. In Traffic Protective Conditions, 366 I.C.C. 112 (1982),11/ the Commission removed these conditions, finding generally that they prevented carriers from offering the cheapest, most efficient service and kept rates artifically high. Notably, the Commission found that interchange costs related to interlining may outweigh costs associated with greater circuity, and therefore, that a longer single line route was not necessarily unlawful. The Commission also addressed the potential problem that carriers would use this new freedom to cancel routes to obtain monopoly rates. It noted that there usually is ample competition from other modes to prevent monopoly pricing. However, if market dominance existed, we would have reasonableness jurisidiction over the rate level as well as §10705 authority to prescribe joint rates.

C. Carrier Actions. Soon after passage of the Staggers Act, the carriers began to implement the new flexibility through their rate structures. Conrail was perhaps the most active, beginning a surcharge program in early 1981. In addition to imposing numerous §10705a surcharges, Conrail also proposed in mid-1981 to cancel many joint rates over particular routes and restrict routing for others. The Commission investigated some of these proposals.12/ Our policy on §10705(e) cancellations has

11/ The U.S. Court of Appeals, 6th Circuit, has stayed the decision pending judicial review. No. 82-3251, Detroit, Toledo & Ironton Railroad Company v. I.C.C., decision of May 19, 1982.

12/ Routing Provisions-Conrail-July, 1981, 365 I.C.C. 753, 759 (1982), remanded, Chesapeake and Ohio Railway Co., et al. v. I.C.C., 704 F.2d 373 (D.C. Cir., 1983). Remand directed to question of representativeness of evidence. Restructured Rates on Recycables-Conrail, 365 I.C.C. 596 (1982), remanded as to connecting carriers' compliance with Section 204 of the Staggers Act in National Association of Recycling Industries, Inc., v. I.C.C., 704 F.2d 636 (D.C. Cir. 1983). Restructured Rates on Grain and Grain Products, Conrail, (Grain), 365 I.C.C. 935 (1982), appeal dismissed for lack of jurisdiction in N.Y. Dock Ry. v. U.S., 696 F.2d 32 (2d Cir., 1982).

evolved through these investigations and later adjudications.13/ These cases balance the statutory goals of the public interest, carrier efficiency and revenue adequacy.

Conrail's actions have been notable not only because of their breadth but because Conrail also undertook to revise entirely its rate structure on the affected movements. For example, in the Grain case adjustment, Conrail established a new rate structure dependent upon the extent of its ability to handle the traffic. The new rates (whether single line or proportional)14/ were designed to recapture traffic, much of which had been lost to trucks due to noncompetitive rail rates.

Beginning in late 1981 and early 1982, other carriers began similar programs, typically targeting particular commodities. As a general proposition, these actions comport with the Staggers Act mandate. That is, rail carriers are no longer acting in concert, offering equal opportunities for all regardless of location, management efficiency or other variables, but instead are being operated as individual businesses, run to make the most of what each has to offer the shipping public.

It is not surprising that one result of this industry about-face on the prior joint rate-open routing practice would be a corresponding change in approach to a by-product of it--reciprocal switching.

The rate structure for reciprocal switching was, for many carriers, in need of revision. In part because these rates were rarely, if ever, subject to general rate increases, they tended to be very low and in some cases may not even have covered marginal cost. Therefore, we see carriers critically evaluating the cost and benefits of reciprocal switching on the basis of

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13/ E.g. Joint Line Cancellation-Soda Ash-UP R. Co., 365 I.C.C. 951 (1982). (Soda Ash)

14/ When a joint rate is cancelled, local or proportional rates will apply, at the least for the cancelling carrier's portion of the movement. A local rate carries no restrictions on its use with other rates. A proportional rate is restricted to use in combination with a prior or subsequent movement. It is often necessary for the other carriers involved in the movement to reassess their connecting local rates, determine whether they are competitive in combination with the cancelling carrier's new rates, and make adjustments based on marketing considerations. See Routing Provisions-Conrail-July, 1981, 365 I.C.C. at 649-650.

individual markets. We cannot conclude that this type of behavior is anticompetitive per se. We have yet to see a situation where a shipper did not have recourse to an alternate commercial switching rate or a line haul rate or other competitive alternative. Of course, where the Commission otherwise has jurisdiction over the remaining rate, a complaint case may be brought to test that rate's reasonableness.

THE PETITION

The above discussion reflects our experience to date with the evolving structure of joint rates and reciprocal switching.15/ It is in this context that the NITL petition and supporting statements must be analyzed.

Overall, NITL does not point to particular anticompetitive results. It appears to assume that activities limiting joint rate application and use of existing market power are anticompetitive per se. As should be clear from the prior discussion, we disagree with this underlying premise. See also Ex Parte No. 427, Joint Rates Study, not printed, served November 18, 1982. Certain comments also seem to imply that the shipper's statutory right to route includes the right to the same rate over different routes. Virtually all shippers and carriers express a preference for the relative simplicity of joint rates (compared to proportional rates) and the service alternatives that exist when many routes are available.

In our view, however, it is not the number of routes alone that constitutes competition, but also the competitiveness of the alternatives. Moreover, as discussed earlier, rate disparities among routes are not unlawful, per se.

15/ See Finance Docket No. 29908, Delaware & Hudson Railway Co. and New York Department of Transportation - Exemption for Use of Terminal Facilities, not printed, decision served May 3, 1983; Delaware & H. Ry. Co. v. Consolidated Rail Corp., 366 I.C.C. 845 (1982); Finance Docket No. 29831, Western Kentucky Trucking Co., Inc., Louisville and Nashville Railroad Co. and Illinois Central Gulf Railroad Co. -- Reciprocal Switching Agreement, not printed, decision of Division 2 served May 13, 1983; No. 38[illegible]1, Central States Enterprises, Inc. v. Seaboard Coast Line Railroad Co., et al., not printed, initial decision served February 1, 1983; and No. 39021, Midtec Paper Corp., et al. v. Chicago & North Western Transportation Co. (Use of Terminal Facilities and Reciprocal Switching Agreement), not printed, initial decision served April 29, 1983. In the first three cases, the relief was granted; in the last two it was denied.

To the extent that recent changes to the joint rate structure reflect inherent or developed advantages one carrier may have over another, such as a shorter or more efficient single line route, they are changes that the Staggers Act encourages, as they ultimately produce a more efficient and competitive industry. A similar conclusion is required to the extent switching charges begin to reflect cost as well as particular competitive conditions. If revenue adequacy is to be attained, or stockholders satisfied, carriers need to pursue the opportunities available under the statute.16/ Indeed, part of the Commission's role is to encourage carriers in these pursuits. See, e.g., §10101a. Ultimately, the public interest is served.

There are, and will continue to be, some uncertainties, dislocations and other problems for individual shippers and carriers. This will be true during any transition.

We are and will continue to be sensitive to situations where one party may wield an unfair advantage over another party without losing sight of the broader goals of the statute.17/ There are existing remedies available to shippers and carriers to address such individual wrongs. While the comments indicate a high level of sophistication in this area, a few brief comments may be in order.

First, certain parties question the right of carriers to effect numerous rate and route changes in one action. We have held that the Act does not prohibit broad actions, but that a

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16/ For the most part, our review of these activities indicates, however, that carriers are extremely sensitive to the effects of rate and routing adjustments on their shippers. Typically, their actions include adjustments that reflect the circumstances of valued shippers. See letter from Conrail, dated April 20, 1983. It may not be assumed that railroads will behave irrationally and drive attractive traffic off the system. However, we recognize that essentially ministerial functions may be made more difficult (e.g., rate determination, bill of lading preparation). These practical problems will also be addressed in our study.

17/ In fact, we have suspended and set for investigation those proposals where there is the probability of unlawfulness. See e.g., I&S No. 9260, Restriction of Reciprocal Switching, Pulp, Paper and Coal, Conrail; I&S No. 9261, Restricted Application of Single-Factor Joint Rates, Southern Pacific; and I&S No. 9262, same title. In all these cases, the carriers voluntarily cancelled the suspended matter, in one case prior to our action.

representative showing is necessary. Routing Provisions-Conrail-July, 1981, supra. The reviewing court affirmed this analysis, it is consistent with §10701a(a), and piece-by-piece activity would unnecessarily delay otherwise lawful changes.

Second, in response to comments submitted by the Soo Line, we reject the argument that a cancellation must be found unlawful if it has the effect of nullifying a contract with an intermediate carrier. See Chesapeake and Ohio Railway Co., et al. v. I.C.C., supra. The carrier cancelling the joint rate is not a party to the contract and, thus, has no legal obligation to abide by it. The statutory standards for joint rate cancellation include consideration of the contract issue in connection with the required analysis of the impact on affected shippers and carriers.

Most important to our §10705 and 11103 analysis is, however, the fact that the existing statutory criteria require case-by-case analysis of individual fact patterns which will reflect different economic and competitive circumstances in each case.[18/] As found in Cancellation of Intermediate Routing, Michigan N. Ry., 365 I.C.C. 51 (1981), what may appear on the surface to be anticompetitive conduct may simply be a reasoned and justifiable business response.

Because of the importance of the specific facts in each case, the provisions of §10705(e), §10705a and §11103 cannot usefully be interpreted in the broad sense NITL seeks.[19/] It would be administratively impractical, via a general rulemaking, to state categorically which actions are lawful and which are not. We are not prepared at this time to attempt to propose or

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18/ We have seen few protests that contain convincing, particularized data addressing the statutory criteria. We again direct the parties' attention to the various §10705(e) cases cited here. Those cases discuss in detail the type of evidence that will satisfy the statutory tests.

19/ For example, §10705(e) directs us to consider: (1) the distance traveled and the average transportation time using the various routes preferred by opposing parties; (2) effects of the cancellation on energy consumption; and (3) the impacts of cancellation on affected shippers and carriers. This requires an extremely complicated and detailed study (including cost data) of routing prior to and after the adjustment to determine, in effect, whether different routes are natural competitors or if prior routings were competitive solely because of the arbitrary and non-cost based, open routing/rate equalization practice.

adopt new standards nor would it serve any real purpose to reiterate the existing standards of review discussed in this decision.

Finally, we note that complaints may always be filed. This avenue lends itself to the in-depth analysis of unique fact patterns required by the statute. Indeed, some parties to this proceeding have already filed such complaints and they are going forward. We will require corrective action in a particular case if warranted.

SUMMARY OF THE STATUTORY SCHEME AS IT RELATES TO THE PETITION

In the 4R and Staggers Acts, Congress struck a balance between railroad revenue need and protection of captive shippers. Recognizing that rail assets are relatively fixed, revenue adequacy can only be reached by each carrier using its particular resources and avantages. The Interstate Commerce Act considered as a whole clearly reflects a Congressional understanding that exercise of rail market power is not per se unlawful.[20/] Differential pricing, reflecting supply and demand, must be permitted if a private sector rail industry is to survive. See Ex Parte No. 347 (Sub-No. 1), Coal Rate Guidelines--Nationwide, notice of proposed rulemaking served February 24, 1983. Market power, where it exists, will in most cases ultimately be controlled through our jurisdiction over the rate level for captive traffic.

The Commission should not unnecessarily expand the limitations imposed by the statute and should instead allow each carrier all possible freedom to structure its own pricing, service and other competitive responses. See §10707a(h). We are to intervene only when there are inadequate economic restraints on market power. Accordingly, we may not consider §10705(e), §11103, or any other provision in a vacuum. For example, it may be inconsistent for us to require maintenance of a particular joint rate if the involved traffic is subject to sufficient competitive pressure to restrain rail market power overall. As we discussed in Ex Parte No. 320 (Sub-No. 20), Market Dominance Determinations, 365 I.C.C. 118 (1981),[21/] these pressures take

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[20/] See §10709 and 10505.

[21/] Remanded, Western Coal Traffic League, et al. v. I.C.C., 649 F.2d 378 (5th Cir. 1982), rehearing en banc granted March 7, 1983.

many forms, and require individualized analysis. Thus, before we may exercise our discretion to prevent route or rate adjustment or require reciprocal switching, we should be confident that our intervention is necessary because natural competitive pressures do not exist or are insufficient to produce economically rational pricing or service.

CONCLUSION

There is no doubt that the Staggers Act has had a significant effect on rail pricing and service. It has ushered in a new era of railroad flexibility and reduced regulation. The changes Congress sought to effect are not without transition cost. As we have said in a number of other contexts, Staggers Act created a new way of doing business in the rail industry. Many of the restraints on rail pricing and behavior have been removed. An important part of these changes is the increased ability of rail carriers to set the terms of their participation in joint line arrangements.

We view our role in this transition seriously. The Commission is to facilitate change to a less-regulated environment, and to provide remedies should carriers abuse their new freedoms.

To assist in both these roles, the Commission has initiated an industry-wide study of the activities with which the parties here are concerned. The study will be based on an in-depth analysis of the causes and effects of these carrier actions. It will be designed to: (1) assess the impact of these changes on individual shippers and the system as a whole; and (2) analyze them in light of the policies and provisions of the statute. If needed, we will seek further public comment on particular issues. We will use the results of the study and any comments we may request to determine the need for further action on our part. It should be useful, as well, in connection with oversight hearings on the Staggers Act, and our continuing review of joint rates in connection with Ex Parte No. 427, supra. We believe this approach will be far more useful than attempting to establish new standards through a rulemaking and, in conjunction

with ongoing adjudications, should address the concerns expressed by many commentors--concerns which we share.

The petition is denied.

This decision will not significantly affect either the quality of the human environment or conservation of energy resources.

Decided: June 27, 1983.

By the Commission, Chairman Taylor, Vice Chairman Sterrett, Commissioners Andre and Gradison. Chairman Taylor concurring in part, dissenting in part with a separate expression.

(SEAL)

Agatha L. Mergenovich
Secretary

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CHAIRMAN TAYLOR, concurring in part, dissenting in part:

In disposing of the NITL petition, a majority of the Commission categorically states that cancellations of joint rates and reciprocal switching can only be analyzed in individual adjudications after a careful examination of the facts in each case. The same rationale is applied to the Commission's ability under 49 U.S.C. 11103(c)(1) to require carriers to enter into reciprocal switching arrangements, where such agreements are found practicable and in the public interest.

I agree with the general theme of the majority's position, i.e., that the law must be applied in individual adjudications. However, I believe that public comments on the issues raised by the NITL would be useful and would ultimately aid the Commission in the adjudication of individual joint rate and reciprocal switching cancellations. Such comments would also help us determine our general powers under 49 U.S.C. 11301(c)(1).

On the subject of joint rate cancellations, the majority appears to be signaling a move toward the elimination of any consideration of the specific standards contained in 49 U.S.C. 10705(e) by concentrating its analysis solely on the

reasonableness of the resulting proportional or local rates. The majority decision relies upon 49 U.S.C. 10707a(h) and the emphasis of the Staggers Act on railroad revenue adequacy as support. I am not so certain of this course and would have preferred to explore this subject by the solicitation of public comments. The Staggers Act did not specifically modify section 10705(e) to allow greater flexibility in joint rate cancellations. By enacting 49 U.S.C. 10705a, Congress only created greater, not unfettered flexibility for the lowest revenue to variable cost traffic.

Congress also enacted section 11103(c)(1) to encourage the expansion of competitive rail service where a possibility exists that competition might be reduced by subsequent joint rate cancellations or by the operation of other provisions of the Staggers Act. H.R. Rep. No. 96-1035, 96th Cong. 2nd Session 67 (1980). How does section 11103(c)(1) relate to criteria for allowing the cancellation of reciprocal switching arrangements? Should the Commission look only at the reasonableness of the resulting switching charge or at other factors? Comments on these questions would be helpful, because too few cases have been handled at the formal level for the majority to make categorical statements concerning the "law" of cancellation of reciprocal switching. Generally speaking, reciprocal switching can be regarded as pro-competitive, and as a result, the reduction of its availability should be carefully examined.

The Staggers Act focused on eliminating unnecessary regulation and increasing railroad revenues to adequate levels. However, especially in the sensitive area of joint rate cancellations and reciprocal switching, it appears that Congress sought to balance the need for competition and adequate revenue levels with the maintenance of an efficient and properly coordinated national rail system. I had hoped a public proceeding would explore these goals and the tools available to

APPENDIX

Replies in support of the NITL petitions were filed by:

Aerospace Industries of America, Inc.

American Paper Institute, Inc.

The Chlorine Institute, Inc.

Dow Chemical Company

Ethyl Corporation

FMC Corporation

Monsanto Company

Occidental Chemical Corporation

PPG Industries Inc.

Bartlett Agri Enterprises, Inc.

Pennwalt Corporation

International Minerals & Chemical Corporation

Anchor Hocking Corporation

Farm Industrial Equipment Institute

National Grain and Feed Association

The Fertilizer Institute

The Procter & Gamble Company

Southern Hardwood Traffic Association

Allied Chemical Corporation

Sun Refining and Marketing Company

LCP Chemicals & Plastics, Inc.

American Petroleum Institute

Chemical Manufacturers Association

Owens-Illinois, Inc.

National Steel Corporation

Institute of Scrap Iron & Steel, Inc.

Rubber Manufacturers Association, Transportation Committee

Society of the Plastic Industry, Inc., Committee on Transportation and Distribution

American Feed Manufacturers Association

the Commission to strike the balance sought by Congress. In my opinion, such an inquiry would have greatly assisted our adjudication of subsequent proceedings.

I also believe these questions should be addressed now and not at some unspecified time hereafter within the context of a staff study on the effects of joint rate and reciprocal switching cancellations. Moreover, the staff's analytical efforts should not be compromised by the incorporation of somewhat questionable interpretations of statutory intent. In any event, such a staff study should be a supplement to and not a substitute for a thorough examination of the highly important policy questions raised by the NITL petition.

Served October 19, 1983

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INTERSTATE COMMERCE COMMISSION

FINANCE DOCKET NO. 29802

DELAWARE AND HUDSON RAILWAY COMPANY v. CONSOLIDATED RAIL CORPORATION—RECIPROCAL SWITCHING AGREEMENT

FINANCE DOCKET NO. 29802

DELAWARE AND HUDSON RAILWAY COMPANY v. CONSOLIDATED RAIL CORPORATION—RECIPROCAL SWITCHING AGREEMENT

Decided October 12, 1983

Prior decision, 366 I.C.C. 845, supplemented and affirmed. Reciprocal switching agreement required under 49 U.S.C. 11103(c) because it is practicable and in the public interest and because it is required to provide competitive rail service.

Charles N. Marshall, Barbara W. Mather, and *Thomas E. Zemaitis* for Consolidated Rail Corporation.

Eric M. Hocky, George H. Kleinberger, and *William P. Quinn* for Delaware and Hudson Railway Company.

Richard S.M. Emrich for Farmers Export Company and Farmers Export Incorporated.

John D. Heffner for the Philadelphia Belt Line Railroad Company.

DECISION

BY THE COMMISSION:[1]

BACKGROUND AND PRELIMINARY MATTERS

On December 7, 1981, the Delaware and Hudson Railway Company (D&H) filed a petition under 49 U.S.C. 11103(c) seeking imposition of a reciprocal switching agreement between D&H and Consolidated Rail Corporation (Conrail) covering rail service within the city of Philadelphia, PA. Twenty-three verified statements were filed in support of the petition and the Philadelphia Belt Line Railroad Company (PBL) intervened in support of the petition. In the prior decision, *Delaware & H. Ry. Co.* v. *Consolidated Rail Corp.*, 366 I.C.C. 845 (1982), Review Board Number 3 granted the requested relief. Conrail filed an administrative appeal, and D&H and PBL replied. Farmers Export Company

[1] Pursuant to 49 CFR 1011.2(b), this proceeding has been certified to the Commission because it raises important issues regarding the reciprocal switching provisions of 49 U.S.C. 11103(c) which have not been considered by the full Commission and which have a significant impact on rail transportation for shippers in a large geographical area. This renders moot the request of Consolidated Rail Corporation (Conrail) for a decision by the full Commission at this stage of the proceeding.

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and its wholly owned subsidiary Farmers Export Incorporated (collectively Farmers Export) filed a petition to intervene and tendered a reply to Conrail's appeal. Conrail replied to the petition.

Farmers Export's petition for intervention will be granted. A management change at Farmers Export during the initial stage of this proceeding prevented earlier participation. See *United Parcel Service Inc. Ext.—48 States*, 120 M.C.C. 747 (1974). Moreover, Conrail states that it does not object to Farmers Export's participation.

However, Conrail moves to strike Farmers Export's reply to its appeal on the grounds that the reply introduces new, unverified evidence regarding Conrail's cancellation of certain joint rates and the resulting rates. Conrail argues that the material is outside the scope of this proceeding. Because these rate activities are subject to official notice and are probative of the relevant issue of needed rail service at Philadelphia and because Conrail has replied to this evidence, Conrail's motion to strike is denied.

The review board found that the requested reciprocal switching agreement is required under the provisions of section 11103(c) because the proposed service is practicable and in the public interest and is necessary to provide competitive rail service at Philadelphia. On appeal, Conrail contends that the board erred in finding the proposed operations practicable in view of Conrail's evidence showing that the Philadelphia terminal is a disjointed combination of operations of the defunct Penn Central and Reading railroads and is not readily adaptable to the switching operations of another carrier. Conrail further argues that the board erred as a matter of law by considering only intramodal rail competition in finding the proposed service necessary to provide effective rail competition.

Finally, Conrail contends that the board's decision erroneously ignores the United States Railway Association's (USRA) rationale for excluding D&H's direct service to Philadelphia under the Final System Plan (FSP).[2]

Pursuant to 49 U.S.C. 10327(j) we are extending the date for deciding this case from July 5, 1983 to October 20, 1983. The issues presented in this case are of first impression, and a careful analysis of the facts and law are required.

Discussion and Conclusions

The record supports affirmance of the review board's conclusions. Section 11103(c) was created by section 223 of the Staggers Rail Act of 1980, Public Law 96-448 (Staggers Act). Section 11103(c)(1) provides that:

[2]Pursuant to section 206 of the Regional Rail Reorganization Act of 1973 (3R Act), Public Law 93-236.

The Commission may require rail carriers to enter into reciprocal switching agreements, where it finds such agreements to be practicable and in the public interest, or where such agreements are necessary to provide competitive rail service. The carriers entering into such an agreement shall establish the conditions and compensation applicable to such agreement, but, if the carriers cannot agree upon such conditions and compensation within a reasonable period of time, the Commission may establish such conditions and compensation.

Section 11103(c) establishes two disjunctive tests for Commission authorizations of reciprocal switching relief. Relief may be granted under either the "practicable/public interest" test or under the "necessary competitive rail service" test. The record in this proceeding demonstrates that the proposed reciprocal switching agreement is required under both standards.

PRACTICABLE/PUBLIC INTEREST TEST

The Conference Committee report on the Staggers Act states that the standard of "practicable and in the public interest" under section 11103(c) is the same standard the Commission has applied in considering whether to order the joint use of terminal facilities under 49 U.S.C. 11103(a) (formerly 49 U.S.C. 3(5)). See H.R. Rept. 96-1430, 96th Cong., 2d sess. 116 (1980). The Commission exercises its authority to order joint use of terminal facilities when it finds that such use would be in the public interest, would be practicable, and would not substantially impair the carrier owning or entitled to enjoyment of the facilities to handle its own business. See for example *Jamestown, N.Y., C. of C.* v. *Jamestown, W. & N. W. R. Co.*, 195 I.C.C. 289, 292 (1933).

In determining what is "in the public interest," the Commission considers not only the interests of particular shippers at or near the terminal in question, but also the interests of the carriers and the general public. See *Jamestown, supra.* Moreover, an affirmative finding that joint terminal use is in the public interest requires a showing of "some actual necessity or compelling reason," meaning that "more than a mere desire on the part of shippers or other interested parties for something that would be convenient or desirable to them" must be shown. See *Jamestown, supra*, at p. 291 and Finance Docket No. 29908, *Delaware & Hudson Railway Company and New York Department of Transportation—Exemption for Use of Terminal Facilities* (not printed), served May 3, 1983.

Consistent with the Commission's traditional analysis of joint terminal use requests, the review board specified four criteria for determining whether the proposed switching service is practicable and in the public interest: (1) interchange and switching must be feasible; (2) the terminal facilities must be able to accommodate the traffic of both competing car-

iers; (3) the presence of reciprocal switching must not unduly hamper he ability of either carrier to serve its shippers; and (4) the benefits to shippers from improved service or reduced rates must outweigh detriments, if any, to either carrier. See the board's decision, *supra*, 366 I.C.C. at p. 848.

Conrail does not dispute the propriety of the board's criteria. Rather, Conrail challenges the board's application of the criteria.

Practicability and impact on Conrail.—Conrail argues that the board did not properly address its evidence showing that the proposed switching operations within Philadelphia are impractical and inefficient. Conrail's Philadelphia terminal is a combination of the facilities of the Penn Central and Reading railroads which were direct competitors and which, consequently, maintained separate and essentially incompatible systems to serve shippers. Conrail states that it has improved the efficiency of the Philadelphia terminal by concentrating traffic classification operations outside of Philadelphia and thus has eliminated the use of a substantial number of runner crews previously employed to carry traffic from, to, and within the Philadelphia terminal.

At present, almost all of Conrail's Philadelphia-bound traffic originating north and west of the city, such as the considered D&H traffic, moves through Enola, PA, for blocking operations. Direct movements are then made from Enola to the final serving terminals in Philadelphia. Conrail argues that introduction of D&H's reciprocal switching operations within Philadelphia at West Falls Yard will require reinstitution of runner crews at the Philadelphia terminal to move traffic between West Falls and the final serving yards. It contends that the resulting intraterminal movements will be circuitous because of the disjointed nature of the Philadelphia facilities.

Moreover, Conrail states that the inefficiency of D&H's operation is compounded because Amtrak succeeded to the main-line tracks through Philadelphia rather than Conrail. Conrail avoids using Amtrak's line whenever possible because of the substantial expense which it incurs combined with the low priority assigned to its freight service.

Finally, Conrail contends that the increased costs involved in the proposed operations are economically prohibitive. It argues that these costs will place an undue burden on it and the shipping public.

Conrail's arguments are not persuasive. The board correctly found that most of Conrail's trains between Enola and Philadelphia are operated on the former Reading line passing through West Falls Yard to Belmont Station. The record shows an entirely feasible connection between former Reading and Penn Central lines through Belmont Station. Additionally, the record shows that certain Conrail traffic destined to Philadelphia

from the Allentown area is routed via Abrams Yard at Bridgeport, PA, and is then moved to Philadelphia by trains set out and picked up at West Falls. This is a practical route for the considered traffic. Thus, the record shows that feasible routings exist for the involved reciprocal switching movements.

The record further shows that Conrail operates six yard crews at West Falls Yard which travel between West Falls and final serving yards such as the Port Richmond, South Philadelphia, and 44th Street Yards. Conrail's contentions concerning the reinstitution of runner crews is more a matter of job assignment than job creation. The record shows that Conrail's Philadelphia terminal operations are fully capable of handling the proposed reciprocal switching.

Conrail's arguments are further undercut because it currently conducts reciprocal switching operations with the Chessie System at the Philadelphia terminal for traffic originating south of Philadelphia. The record fails to show operational problems stemming from this switching service. On the contrary, Conrail argues strongly that Chessie is an effective competitor for Philadelphia traffic as a result of the efficient switching operation.

Conrail's arguments concerning increased costs are speculative and premature. D&H's operating suggestions such as preblocking of its cars before delivery to West Falls could eliminate substantial economic burdens. D&H further suggests that runner crews may not be needed to serve points in South Philadelphia from West Falls Yard, because through trains currently operating from Harrisburg through West Falls could pick up D&H cars there and set them off at points in South Philadelphia.[3]

Moreover, Conrail will be remunerated for its switching costs under the agreement to be negotiated pursuant to this decision. As to increased shipper costs, it will be D&H's ability to absorb Conrail's switching costs which will determine whether shippers will use D&H's service. If D&H cannot absorb sufficiently the cost of switching, it will not move traffic. However, because Conrail and Chessie have arranged and are performing reciprocal switching at Philadelphia for traffic from and to points south of the city, there is every reason to conclude that Conrail and D&H can also agree upon and successfully conduct switching operations and perform a practicable service at competitive rates.

Therefore, we find that the proposed operation is practicable and will not adversely effect Conrail's operations.

[3] Conrail alleges that this proposal runs afoul of its labor agreements which prohibit trains operated by road crews from picking up and setting off the same cars within the Philadelphia terminal area. However, Conrail fails to specify the involved labor agreement provisions. In any event, D&H's suggestion is not critical to the feasibility of the proposed service.

Public interest.—Any detriment incurred by Conrail from D&H's service is far outweighed by the substantial benefits enuring to the public from the proposed operation. Conrail attempts to downplay these benefits, arguing that the board's affirmative conclusion on the issue of public interest is based on the assertedly arbitrary assumption that access to an alternative rail carrier will necessarily benefit shippers by creating the potential for better service and lower rates.

We disagree with Conrail. Additional rail competition is a clear public benefit from the proposed operation, one which is endorsed by rail transportation policy announced in the Staggers Act.[4] Under the Staggers Act, competition is normally presumed to be in the public interest, and the proponent bears a light burden on this issue. In *Chicago & N. W. Transp. Co.—Construction*, 363 I.C.C. 906, 927 (1981), we stated in an analogous context:

> We agree that the existence of an additional rail carrier is likely to result in more efficient and responsive service than that currently available. We also agree that competition will have a moderating influence on rates and that those rates should be lower than those that would apply in the absence of competition.

Moreover, the record also demonstrates a compelling public need for D&H's service. Under the FSP most Philadelphia-based shippers are captive to Conrail for necessary rail service. The review board cited several instances of the supporting firms' need for additional rail service for improved rates and equipment utilization. For example, Nabisco Brands, Inc., Special Products Division, receives flour in rail hopper cars at one of its major bakeries at Philadelphia and holds itself out to ship finished bakery products via the mode selected by its customers. It states that D&H's service will ensure an adequate supply of hopper car equipment for inbound traffic and at the same time enable it to obtain reduced carload rates competitive with motor carrier rates.

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[4] Of particular relevance are the following portions of the rail transportation policy set forth in section 101 of the Staggers Act and now embodied in 49 U.S.C. 10101a:

> In regulating the railroad industry, it is the policy of the United States Government—
>
> (1) to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail;
>
> . . . . . .
>
> (4) to ensure the development and continuation of a sound rail transportation system with effective competition among rail carriers and with other modes, to meet the needs of the public and the national defense;

The proposed service is consistent with these objectives.

Intervenor Farmers Export, a Kansas-based agricultural cooperative, leases a grain elevator from Conrail at Port Richmond which is within the Philadelphia terminal. It states that D&H's operations will enable it to gain access to grain supplies on lines other than Conrail and to obtain competitive rail rates at Philadelphia so that it can effectively compete with other grain exporters which use other eastern port facilities. It points out that, subsequent to its leasing the Port Richmond facility, Conrail refused to concur in reduced joint rates on traffic originating on the lines of the Baltimore and Ohio Railroad Company (B&O) and the Norfolk and Western Railway Company (N&W), even though Conrail had reduced its own single-line rate applicable from its origins. It contends that Conrail's joint rate cancellations have effectively cut off its Port Richmond facility from any grain sources other than those on Conrail's lines. D&H's service will provide Farmers Export with increased sources of supply and competitive rail rates and service.

Moreover, in considering the interests of the carriers and general public in determining the "public interest," we note that in *Guilford Transp. Industries, Inc.—Control—D&H Ry. Co.*, 366 I.C.C. 396 (1982) we authorized the control of D&H by Guilford Transportation Industries, Inc., finding that the "primary benefit of the proposed transaction is the lifeline it will provide to the ailing D&H." *Id.* at p. 400. The improvement in D&H's financial picture brought about by Guilford's control will be further enhanced by authorization of reciprocal switching operations in Philadelphia.

Furthermore, intervenor PBL, a class III carrier serving 16 Philadelphia shippers and the port of Philadelphia, states that the lack of competitive rail service has kept rates artificially high, diverted substantial traffic to other ports and plants in other cities, and caused former Philadelphia area industries to relocate to other cities. PBL cites section 1166 of the Northeast Rail Service Act of 1981, Public Law 97-35 (Subchapter E of Title XI), as a clear indication that Congress recognized the need for additional rail service within Philadelphia:

> At any time after the effective date of this subtitle, the Commission may approve under provisions of existing law, the grant of trackage rights to any terminal railroad operating primarily in the City of Philadelphia over the individual lines of Conrail located in the City and port of Philadelphia.

The cumulative record demonstrates a compelling public need for the considered service.

Conrail argues, however, that the board did not properly consider the public interest because USRA declined to provide D&H with direct access to Philadelphia in the FSP. Specifically, Conrail cites the Special

Court decision in *Consolidated Rail Corp.* v. *Delaware & Hudson Ry.*, 543 F. Supp. 1079, 1082-83 (Sp. Ct. RRRA 1982), where the court stated:

> It is expected that in applying [the] criteria [of section 11103(c)(1)] the ICC will take into consideration, among other things, whether the agreement here proposed by D&H would unduly weaken Conrail and thereby jeopardize a sizeable public investment and that the ICC will also take into account that the USRA notwithstanding the directive with respect to competition in RRRA [3R Act] §206(a)(5), declined to afford D&H direct entry into Philadelphia * * *.[5]

Conrail also argues that the board erred in finding D&H's right to interchange traffic under the FSP includes the right to interchange traffic in reciprocal switching operations at Philadelphia. It states that D&H's "overhead rights" do not include pickup and delivery service attendant to the considered reciprocal switching service.

Conrail's arguments do not require a reversal of the board's decision. First, Conrail does not contest the Special Court's basic determination that the FSP does not preclude our jurisdiction to consider D&H's petition for reciprocal switching under section 11103(c). This conclusion is underscored by findings of the Special Court:

> The notion that Congress conceived of RRRA as granting properties conveyed thereunder complete immunity from future adverse development as the result of ICC action under new or existing legislation is unacceptable as a matter of both language and good sense. Equally unacceptable is the notion that the pattern of rail service established by the FSP can be altered only by supplemental transactions pursuant to §305 [of the 3R Act] and not by proceedings under legislation of general applicability.

See *Consolidated Rail Corp.* v. *Delaware & Hudson Ry.*, *supra*, at p. 1083. Thus, any error committed by the board in concluding that D&H's proposed reciprocal switching rights are subsumed by its FSP overhead rights is harmless, because such error does not alter the disposition of this proceeding.

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[5] Section 206(a) of the 3R Act states in pertinent part:

> The final system plan shall be formulated in such a way as to effectuate the following goals:
>
> (1) the creation, through a process of reorganization, of a financially self-sustaining rail and express service system in the region;
>
> (2) the establishment and maintainance of a rail service system adequate to meet the rail transportation needs and service requirements of the region;
>
> . . . . . .
>
> (4) the preservation, to the extent consistent with other goals of existing patterns of service by railroads * * *; [and]
>
> (5) the retention and promotion of competition in the provision of rail and other transportation services in the region * * *

Moreover, the board considered the possible impact of the proposed operations on Conrail. Conrail does not challenge the board's detailed findings in the prior decision 366 I.C.C. at p. 852 that only up to 6 percent of Conrail's Philadelphia traffic is subject to diversion by D&H's proposed service. Instead, Conrail relies on general allegations that the proposal would have a negative impact on its revenues and operating efficiency. As supplemented here, we affirm the board's finding that the D&H-Conrail reciprocal switching service will not materially adversely affect Conrail. On this record, where Conrail has not quantified the impact of D&H's proposal, we conclude that the proposal will not conflict, to any significant degree, with the goals articulated in section 206 of the 3R Act. Against this background we have balanced the compelling public need demonstrated for D&H's direct Philadelphia service and find that it outweighs any potential detriment to Conrail. Therefore, we are convinced that our decision complies with the concern of the Special Court for the economic health of Conrail.

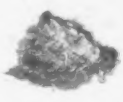
We also acknowledge that, as pointed out by the Special Court, D&H was not given direct access to Philadelphia in the FSP despite the directive in section 206(a)(5) of the 3R Act that competition be promoted. This does not, of course, prevent us from granting such access at this time, as the Special Court made clear in the paragraph quoted directly above.

Several factors have led us to a result differing from the FSP: (1) the increased emphasis by Congress since the FSP on competition in the rail industry, as illustrated generally by the Staggers Act and specifically by section 11103(c) itself as well as section 1166 of the Northeast Rail Service Act of 1981; (2) the improved financial condition of Conrail, permitting it to more effectively respond to new competitors; and (3) the compelling record before us indicating the present need for competitive rail service in Philadelphia, as described in the next section.

Based on the foregoing analysis, we conclude that the proposed reciprocal switching agreement is practicable and in the public interest.

Necessary Competitive Rail Service Test

Because we have concluded that D&H's petition meets the first alternative test of section 11103(c), we need not necessarily find that it meets the second test of "necessary competitive rail service." See *Western Kentucky Trucking Co., Inc. Louisville and Nashville Railroad Company and Illinois Central Gulf Railroad Company—Reciprocal Switching Agreement* (not printed), served May 13, 1983. However, we find that D&H's petition meets both tests, and will address Conrail's arguments on the second statutory standard.



Conrail contends that the board erred in considering only intramodal rail competition in finding that D&H's proposal met the "necessary competitive rail service" test. Conrail states that the board's standard leads to the unreasonable result that a competing carrier will be able to impose a reciprocal switching agreement on serving carriers in every instance where a particular shipper or group of shippers has access to only one carrier.

Conrail analogizes to merger proceedings under 49 U.S.C. 11344 arguing that consideration of the entire transportation market is required to assess properly the need for additional rail competition under section 11103(c). It contends that the "necessary competitive rail service" test under section 11103(c) requires the same intermodal assessment as applied in merger proceedings in determining "whether the proposed transaction would have an adverse effect on competition among rail carriers in the affected region" (49 U.S.C. 11344(b)(1)(E)). It cites several proceedings in which we found that proposed mergers would not adversely affect competition because of the presence of alternative intermodal services.

We affirm the review board's interpretation of the intramodal analysis under the "necessary competitive rail service" test. The clear language and legislative history of section 11103(c) show that it was Congress' intent that we focus on rail-to-rail competition in determining whether reciprocal switching agreements are necessary to provide competitive rail service. As noted by the board in the prior decision, 366 I.C.C. at p. 854, the Senate Report (S. Rept. 96-470, 96th Cong. 1st sess. (1979)) accompanying section 203(b) of Senate Bill No. S. 1946, the forerunner of what ultimately added section 11103(c), states that:

> The new railroad transportation policy established by this bill emphasizes the need for increased intramodal and intermodal competition and section 203 deals with intramodal competition among railroads.

Moreover, the Conference Committee Report of the Staggers Act (H.R. Rept. 96-1430, 96th Cong., 2d sess. 116 (1980)) states the purpose of the reciprocal switching legislation in section 11103(c) and gives a clear indication of the manner in which the legislation is to be applied:

> In areas where reciprocal switching is feasible it provides an avenue of relief for shippers where only one railroad provides service and it is inadequate.

The board's decision is consistent with the legislative history of section 11103(c).

Apart from the legislative history of section 11103(c), Conrail's analogy to the intermodal transportation analysis under the rail consolidation section 11344 is inapposite, because the different purposes of the two sections of the act require different interpretations and administration. The consolidation section is concerned with prohibiting anticompetitive effects while authorizing a diminution of the absolute number of rail carriers. On the other hand, the reciprocal switching section is concerned with increasing rail competition by authorizing an increase in the absolute number of rail carriers serving a particular market. The legislative mandate of section 11103(c) thus requires a narrower (intramodal) focus in determining whether reciprocal switching is necessary to provide "competitive rail service" in a particular market.

Moreover, assuming *arguendo* that we addressed the entire transportation picture (motor as well as rail) under the "necessary competitive rail service" test of section 11103(c), our decision to authorize reciprocal switching would not be altered. Conrail sets forth data showing that motor carriers dominate the transportation of manufactured products to and from Philadelphia. Conrail also asserts that there is substantial competition for transportation of export grain and coal at eastern ports other than Philadelphia. It contends that each of these factors acts to restrain its pricing freedom and compel it to offer low cost, efficient service in order to maintain its Philadelphia traffic.

Conrail's evidence of alternative transportation fails to negate the stronger countervailing evidence of a need for competitive rail service at Philadelphia. D&H's unrebutted evidence shows that substantial volumes of coal and farm products originate and terminate at Philadelphia. For example, in 1980, of the 204,503 total carloads of Philadelphia traffic, 81,518 carloads or 40 percent were comprised of farm products and coal. Much of this traffic is not susceptible to motor transportation; and for shippers such as Farmers Export with facilities at Philadelphia on Conrail's line, interport competition does not lessen the need for effective rail competition.

Conrail argues that effective intramodal rail competition at Philadelphia is provided by the Chessie and also by virtue of Conrail's switch tariff (ICC-CR-3014-A). However, Conrail fails to show the extent of Chessie's competition; and, in any event, the record shows that Chessie competes for southern and western traffic and not for the northern and northwestern traffic at issue here. Furthermore, as found by the board, Conrail's switch tariff is not an example of effective rail competition, because it is subject to cancellation and rate increases particularly in situations where Conrail is moving cars to or from a shipper for whose long-haul traffic Conrail competes, such as in the case of Farmers Export.

Conrail argues that neither D&H nor any of the supporting firms have demonstrated that its pertinent switching rate, or its line-haul rates are unreasonably high. However, the reasonableness of Conrail's rates cannot determine the need for additional rail competition at Philadelphia. As Conrail acknowledges, rail carriers have been given a great deal of flexibility to adjust their rates under the Staggers Act. We are convinced that Congress' aim in creating section 11103(c) of the Staggers Act was to provide a competitive counterbalance to this broadened rate freedom. The Conference Committee's Report on the Staggers Act underscores this finding.

> In general, the title [Title II—Railroad Rates and Inter-Carrier Practices of the Staggers Act] assures railroads substantially more rate freedom than is afforded them under existing law. It continues the policy started under the Railroad Revitalization and Regulatory Reform Act of 1976 of substantially eliminating rate regulation of railroads *where there is effective competition.*
>
> . . . . . .
>
> A number of provisions are included to foster greater competition by simplifying coordination, minor mergers procedures, entry and *reciprocal switching agreements.*

See H.R. Rept. 96-1430, *supra*, at p. 80 [emphasis added].

Based on the foregoing analysis, we affirm the review board's finding that a reciprocal switching agreement between D&H and Conrail for service at Philadelphia not only is practicable and in the public interest but also is necessary to provide competitive rail service.

This decision will not significantly affect the quality of the human environment or the conservation of energy resources.

VICE CHAIRMAN STERRETT, dissenting:

The Commission's decision in this case can be distilled to a single proposition: reciprocal switching will be ordered wherever there is only one rail carrier now providing direct service. Thus the majority has interpreted the statutory prerequisites so loosely as to render them meaningless. This may have broad implications for the rail industry. The practical effect will be to require rail carriers to operate their trains for the benefit of their rail competitors, upon demand. Concomitantly, it will hinder, if not prevent, cancellation of economically burdensome switching agreements. In addition, rail carriers innovative enough to advance into new markets to compete with other modes will face the prospect of having to split with the first rail petitioner to come along whatever gain they might obtain. Ironically, the ultimate result may be to stifle competition rather than encourage it.

This case is also important in that it involves a major modification of the Final System Plan ("FSP")—the congressionally approved, massive restructuring of the Northeast rail system carried out by the United States Railway Association ("USRA") in 1976. While certainly the FSP is not inviolate, it seems to me important for the Commission to give great weight to the reasons USRA chose not to grant the D&H direct entry into Philadelphia. Indeed, the Special Court has admonished the Commission to consider USRA's reasons. It is important to do so if for no other reason than in recognition of the fact that Congress chose to create USRA and embue it with the authority to make such decisions, instead of conferring that power upon the Commission. Thus it should be presumed that there was reposed in USRA special expertise in these matters.

Yet the decision here fails to even discuss the substance of the FSP. Instead of considering the reasons for USRA's decision, the Commission merely offers justifications for its own. Moreover, the majority's decision, although well-intentioned, does not comport with the law, current Commission policy, or the evidence.

Under section 11103(c) the Commission may order rail carriers to enter into reciprocal switching agreements where such agreements are "practicable and in the public interest" or where they are "necessary to provide competitive rail service."

The Conference Committee report on the Staggers Act defines the standard of "practicable and in the public interest" under section 11103(c) as the same standard the Commission has applied in considering whether to order the joint use of terminal facilities under 49 U.S.C. 11103(a) (formally 49 U.S.C. 3(5)). See H.R. Rept. 96-1430, 96th Cong., 2d sess. 116 (1980). Moroever, an affirmative finding that joint terminal use is in the public interest requires a showing of "some actual necessity or compelling reason." *Jamestown, N.Y., C. of C.* v. *Jamestown, W. & N. W. R. Co.*, 195 I.C.C. 289, 292 (1933). A corollary of this requirement is that it must be shown that existing service is inadequate. See *Hastings Commercial Club* v. *Chicago, M. & St. P. Ry. Co.*, 107 I.C.C. 208, 216 (1926), *quoting Manufacturers Assn. of York, Pa.*, v. *Pennsylvania R. Co.*, 73 I.C.C. 40, 49-50 (1922). The legislative history of section 11103(c) clearly demonstrates that Congress intended this long-established standard be applied. Thus the Conference Report on the Staggers Act notes that "* * * where reciprocal switching is feasible, it provides an avenue of relief for shippers where only one railroad provides service *and it is inadequate*." H.R. Rept. 96-1430, 96th Cong., 2d sess. 116 (1980) [emphasis added].

In considering whether the D&H proposal is in the public interest, neither the Commission nor the review board found that Conrail's present service in Philadelphia is inadequate. In fact there appears to be nothing in the record on which such a finding could reasonably be made. Although the Commission's decision refers to testimony by Nabisco Brands, Inc. and Farmers Export Co., it is clear that those parties support the D&H proposal merely because they believe it would be "convenient or desirable to them," a reason that is insufficient to justify Commission approval. See *Jamestown, supra.* Moreover, the allegations of intervenor Philadelphia Belt Line Railroad which are apparently relied upon by the Commission to show a "public need" for D&H service, are unsupported and pure hearsay.[6]

The Commission's finding that the D&H proposal is "necessary to provide competitive rail service" is predicated on a clearly erroneous interpretation of that statutory standard. Specifically, the Commission narrowed the standard to a single test: is there more than one railroad directly available to all shippers in the area. I simply cannot believe Congress intended the Commission to construe the standard so narrowly as to ignore the existence of widespread intermodal competition where in fact it does exist. Clearly, the purpose of providing "competitive rail service" is to ensure that shippers are not subject to an abuse of market power. This theme pervades the Staggers Act. How, then can the Commission reasonably conclude the D&H proposal is "necessary" if there is vigorous competition between Conrail and other providers of transportation in Philadelphia?

The Commission's misinterpretation of the competitive necessity standard in this proceeding is also contrary to the Commission's own policy, as adopted in Ex Parte No. 445, *Standards for Intramodal Rail Competition* (not printed), served July 7, 1983. There, in referring specifically to section 11103, we correctly interpreted the Staggers Act as contemplating Commission intervention in rail carrier pricing, service, and other competitive activities "only when there are inadequate economic restraints on market power." *Id.* at p. 13. Noting that section 11103 cannot be considered "in a vacuum," we emphasized that "* * * before we may exercise our discretion to prevent route or rate adjustment or require reciprocal switching, we should be confident that our intervention is necessary because natural competitive pressures do not exist or are insufficient to produce economically rational pricing or service." *Id.* at p. 14.

[6] It should be noted that Philadelphia Belt Line's allegations are highly suspect as self-serving, in any event, because it too is seeking Commission-ordered reciprocal switching with Conrail in Philadelphia. See Finance Docket No. 30287, *Petition of Philadelphia Belt Line.*

The Commission's attempt to hedge its bets on the competitive necessity standard by concluding that even if intramodal competition is considered, the D&H proposal is still necessary, is not based on substantial evidence. For example, the Commission's statement that "* * * most Philadelphia-based shippers are captive to Conrail for necessary rail service" is unsupported in the record. There is simply no evidence as to whether *any* Philadelphia shippers are "captive" to Conrail as defined by the statute and the Commission's market dominance standards.[7]

Moreover, the Commission's conclusion that the competitive necessity standard is met because in 1980, 40 percent of all Philadelphia rail traffic was comprised of farm products and coal and that "[m]uch of this traffic is not susceptible to motor transportation * * *." is logically flawed. That there is indeed Philadelphia traffic being carried by rail does not mean it is rail-dependent traffic. In fact, it may demonstrate that Conrail is offering competitive rail service in the face of strong competition. For example, it was uncontested that Conrail's revenue-to-variable cost ratio for Philadelphia traffic in 1980 was 114 percent. See Verified Statement of Pleninger at p. 11. This extraordinarily low figure[8] tends to demonstrate the existence of significant competition.

In summary, there is insufficient reason for the Commission to issue an order that will only result in shifting revenue from one railroad to another. In an era of deregulation this seems particularly unwarranted.

It is ordered:

1. The petition for intervention filed by Farmers Export is granted.

2. Conrail's motion to strike Farmers Export's reply to Conrail's administrative appeal is denied.

3. The prior decision, 366 I.C.C. 845, as supplemented by the findings in this decision, is affirmed.

4. D&H and Conrail shall seek in good faith to negotiate an agreement for reciprocal switching at Philadelphia, PA, and shall report to the Secretary of the Interstate Commerce Commission, within 90 days of the date of service of this decision, as to the success of those negotiations and the terms of any agreement that may be negotiated. In the event an agree-

[7] "Market dominance" is defined by the statute as the "absence of effective competition from other carriers or modes of transportation * * *" 49 U.S.C. 10709(a). See also *Market Dominance Determinations*, 365 I.C.C. 118 (1981), revised in part *sub nom., Western Coal Traffic League* v. *United States*, 694 F. 2d 378 (5th Cir. 1982), *reh'g en banc granted*, No. 81-4257 (March 7, 1983).

[8] The significance of this figure is underscored by the fact that in cases where there is little or no competition the Commission is accustomed to seeing rail rates producing revenue-to-variable cost ratios in excess of 200 percent.

ment for any reason cannot be reached, either party may file a petition within 30 days of the expiration of the negotiating period, requesting the Commission to determine just and reasonable conditions and compensation.

5. The time for deciding this case is extended until October 20, 1983, *nunc pro tunc.*

6. This decision is effective on its date of service.

By the Commission, Chairman Taylor, Vice Chairman Sterrett, Commissioners Andre and Gradison. Vice Chairman Sterrett dissented with a separate expression.

AGATHA L. MERGENOVICH,
Secretary.

(SEAL)

367 I.C.C.

Senator DECONCINI. I have about 2 minutes to go cast a vote, so I am going to have to close the hearings at this time, although the record will remain open for a period of 30 days. Thank you for your testimony.

Mr. DEMPSEY. Thank you, Mr. Chairman.

Mr. DONAHUE. Thank you.

Senator DECONCINI. The committee stands adjourned, subject to the call of the Chair.

[Whereupon, at 4:02 p.m., the committee was adjourned.]

APPENDIX

F. H. STOLTZE LAND & LUMBER CO.

Lumber Manufacturers

Box 1429 COLUMBIA FALLS, MONTANA 59912

September 10, 1984

The Honorable Senator Max Baucus
706 Hart Building
Washington, D.C. 20510

Attn: Bob Vogel

Dear Mr. Vogel:

In response to our conversation of 9/5/84, I would like to bring to the attention of your office and Senator Baucus some of the problems we are experiencing due to the Railroad Transportation Contracts as per section 208 of the Staggers Rail Act of 1980.

We operate three (3) sawmills in Western Montana. Two of them are served by the Burlington Northern, while our mill at Dillon, Montana is on a Union Pacific siding. The BN has offered us a contract which is on a rebate basis. They would rebate back to F. H. Stoltze Land & Lumber Company out of Columbia Falls, Montana mill only $100.00 per Boxcar and $150.00 per flat car if we shipped 500 cars or more. Any cars shipping to Colorado would not actually qualify for a rebate but would count toward the total number of railroad cars required.

In order to even comply with the terms of the contract, we would have to increase our rail shipments by over 35%. Even though our mill at Darby is on the BN, we are not being offered a contract for this mill in as much the BN intends to abandon the railroad Spur which extends from Missoula to Darby.

It is general knowledge that the rebate contract the BN offered us is extremely low. Last Tuesday, a customer phoned me and stated the Boise Cascade Corporation was passing the rebate on to their customers from 3 mills in the state of Washington. They offered my customer a rebate of $500.00 per car from 2 of the mills and $600.00 from the 3rd mill in as much as that mill was served by a competing railroad. The rebate amounted to $10.00 per thousand board feet. It amounted

to our customer favoring our competition because they could ship and deliver at a cheaper price. This is unfair competition perpetrated by the railroad.

There have been other rumors of rebates. The Canadians are trucking lumber from Southeast B.C. into Eureka, Montana loading on BN cars. I was told by one Canadian, that the Contract rebate was very lucrative to them and was in excess of $800.00 per car. The "rumor" also presists that to some BN destinations it amounts to $1,200.00 per car. In as much as the Canadian mills already have advantages of a weak Canadian dollar and selling into a U.S. market with a very strong dollar, they have some advantage, combine this with the fact that the British Columbia Provincial Government subsidies their Forest Products Industry by selling the stumpage at very low prices and not on a competitive bid as we do on this side of the border. Then along comes a U.S. railroad and offers the Canadians a much better rebate than they offer U.S. mills especially those who must ship by the BN if they are to ship by rail.

The BN is vertually in a monopolistic position for the Northern Idaho and Western Montana shipper. They do not treat the smaller shipper on an even basis compared to the larger shipper. The contract rebate system as set up in the Staggers Act is unequitable and in essence is in restraint of Trade, giving one business high preferential treatment over another. I hope that the rebate feature of this Act can be rescinded or modified so as to eliminate the features which eliminate competition in our (Forest Products) industry.

I feel the Staggers Act was certainly in the right direction as far as de-regulation goes, but some of the features run contrary to existing features such as the Sherman Anti-Trust Act.

If additional information is requested, please let me know.

Very truly yours,

F.H. STOLTZE LAND & LUMBER CO.

Richard D. Riley

Richard D. Riley
Sales Manager

RDR/hb

STATEMENT OF DAVID BERNSTEIN
ON BEHALF OF

SUNKIST GROWERS, INC.

BEFORE THE COMMITTEE
ON THE JUDICIARY
OF THE UNITED STATES SENATE

IN SUPPORT OF S.2417

My name is David Bernstein and I am Vice President, Fresh Fruit Marketing, Sunkist Growers, Inc. My office address 14130 Riverside Drive, Sherman Oaks, California 91423. I welcome this opportunity to submit a statement voicing our support for the legislation introduced by Senator DeConcini as S. 2417. Although the bill appears to limit application to shippers of bulk commodities such as coal, ore and grain, I believe the principles of this bill would be beneficial to other agricultural commodities, particularly citrus, and I wanted to express our interest in broadening the scope of the legislation for reasons which I will outline hereinafter.

First, let me briefly state what Sunkist is and why we are interested. Sunkist Growers is an agricultural marketing cooperative with a membership of 6,000 growers located in Arizona and in California. Sunkist is the largest private marketer of fresh citrus fruit in the world. In 1983, we shipped over 54 million cartons of fresh citrus fruit to various parts of the United States which works out to over 1 million tons. Some of our biggest markets are located in the eastern part of the United States so we are talking about a high volume, long haul movement of a perishable commodity which we must get to the major markets in good condition and at reasonable prices. Transportation costs are a major item of expense in marketing fresh citrus fruit. In 1983, the transportation charges for our domestic shipments of fresh

fruit amounted to approximately $125,000,000. This is a lot of money and our principal concern at this time is to keep those costs from getting much larger because of monopolistic pricing by a single rail carrier. This is the reason we are interested in Senator DeConcini's bill.

The rail rates for citrus fruit, along with other fresh fruit and vegetables, are exempt from economic regulation by the Interstate Commerce Commission. We are exempt because the Interstate Commerce Commission found that regulation was no longer necessary to control rail rates since there were ample competitive forces among railroads and between the railroads and the motor carriers. Although we have had some difficulties with the railroads since deregulation, particularly with respect to claims for loss and damage, we are not advocating a return to regulation. We hope to encourage competition and rely on that as the regulator of transportation prices which is consistent with the overall purpose of the Staggers Act.

Our concern is that competition has been diminishing over the past several years. Railroad consolidations are rapidly forming super systems such as the Burlington Northern, CSX, Norfolk Southern, UP-MOP, and now the proposed Santa Fe-Southern Pacific. While motor carriers are an important part of our distribution system, they cannot handle the entire volume of our fresh fruit. The most efficient form of long haul transportation involves the use of rail service, either in refrigerated rail cars or in intermodal (piggyback) service. Our use of rail transportation has been steadily increasing during the past five years. This year 40 percent of our interstate traffic will utilize some form of rail transportation, either piggyback or refrigerator car. We anticipate that rail service will account for over 50 percent of our interstate tonnage by 1986. We are now confronted with a situation where the entire growing area in Arizona and California may be served by one railroad if the Santa Fe-SP merger is approved. Without the competitive influence of another major railroad in our shipper area, we are concerned that transportation prices for rail service will become higher,

the service will become worse, and the railroads will pay little, if any, attention to elimination of loss and damage or payment of claims.

An amendment of the Interstate Commerce Act (Staggers Rail Act of 1980) will not do us any good. I understand there are some legislative efforts designed to help the plight of captive shippers who are subject to regulation by the Interstate Commerce Commission. Our commodities, however, are exempt from such regulation so amendments to the Interstate Commerce Act do not address our problem. This is why we are especially gratified that Senator DeConcini is looking to an amendment of the antitrust laws which will make it possible for other railroads, such as the Union Pacific or the Denver, Rio Grande, to obtain trackage rights so that our packing houses will, in effect, be served by several railroads rather than captive to a single railroad.

We note that the commodities listed in this bill are limited to those commodities which are generally associated with bulk commodities heavily, if not solely, dependent on rail transportation. We urge the sponsors of Senator DeConcini's bill and members of the committee to consider broadening the scope of the legislation to include commodities, such as citrus, which require rail transportation at reasonable prices. Sunkist perhaps does not qualify as a captive shipper as that term is used in the transportation industry. Nevertheless, rail transportation is essential for efficient and economical distribution. We should not be subjected to monopoly pricing any more than any other consumer of goods and services.

Efficient transportation of essential commodities such as citrus fruit is clearly in the public interest. Origins in Arizona and California are several thousand miles from many of our principal markets in the East and the South. Rail transportation is the most cost efficient form of long haul transportation. It is also approximately four times more fuel efficient than motor carriers. The use of trailer-on-flat-car

(TOFC) services combines the efficiencies of rail transportation with the flexibility and service of motor carriers enabling fruit to reach distant markets in good condition at reasonable prices. The consumer and the public are the losers if monopolistic prices and lack of competition force more of our traffic to motor carrier. Healthy competition among the railroads is the key to our ability to use rail services advantageously.

It is true that the Interstate Commerce Commission is conducting hearings on the Sante Fe-Southern Pacific merger and that there have been proposals made that trackage rights should be granted to some railroads as a condition of the merger. Sunkist is supporting such conditions in the merger hearings. Nevertheless, past experience with the Commission's rulings on previous merger cases indicates that the concerns of shippers are given very little, if any, consideration and we believe that any relief we may be able to obtain from a monopoly pricing situation must be through legislation such as S. 2417.

STATEMENT OF DR. WESLEY H. LONG, Ph.D.

ON BEHALF OF

THE NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS

TO

THE SUBCOMMITTEE ON THE CONSTITUTION

OF THE COMMITTEE ON THE JUDICIARY

September 18, 1984

Mr. Chairman and members of the Subcommittee. My name is Wesley H. Long. I am a state regulator, a member of the Public Service Commission of the District of Columbia. In that capacity I am responsible for regulating public utilities (electric, gas and communications), that operate within the District of Columbia. I submit this statement on behalf of the National Association of Regulatory Utility Commissioners who collectively regulate the nation's public utilities at the state level. For this Association I chair the Subcommittee on the Staggers Rail Act Implementation.

Utility Commissioners are extremely concerned about the prices electric utilities pay to transport domestic coal because these prices go directly into the cost of electricity and affect almost everyone. Coal is the primary fuel for more than half of this country's electric generation. On a national average, transportation costs account for approximately one-third of the delivered price of coal shipped by rail. Moreover, there are almost no practical alternatives or competing transportation modes, including slurry pipeline, barge or truck, to ship coal to end users. The result is that for half of the coal that utilities transport, they are captive shippers.

A major factor in forcing up the price of coal transport for captive shippers is the Interstate Commerce Commission, whose startling regulatory interpretation of existing law destroys adequate rate protections for captive shippers. In addition, it refuses to regulate rail transportation rates using standards which have any relation to the costs of providing service. I am an economist and I know regulatory double talk when I hear

it. Judicial relief from this nonsense, if successful, could only be obtained through a costly and time consuming process.

Therefore, the National Association of Regulatory Utility Commissioners, as indicated in the attached resolution adopted on March 1, 1984, supports legislative initiatives to address this galling and costly situation. Specifically, we urge the Congress to enact legislation which obtains adequate protections and access to competitive rail service for captive rail shippers and which obtains for consumers fair and reasonable regulation which protects them from exploitation.

We understand that S. 2417 is designed to promote competition in the railroad industry with respect to shipments of bulk commodities. This is accomplished by amending certain antitrust provisions of the Sherman Act so as to make it unlawful for a monopoly railroad to refuse trackage rights to a shipper or another carrier on reasonable terms. The intent, it appears, is to provide shippers who have access to locomotives and boxcars a means to use tracking facilities to reach the tracks of a competing carrier or the destination of shipment.

In essence the legislation provides for "interconnection" and "wheeling" services, to use public utility terms. The concepts are long-standing in public utility regulation. They are practices which have been provided for in the law and have been employed in the regulation of essential facilities of electric and communications utilities. Therefore, there is ample precedent.

Moreover, interconnections and wheeling make essential services more available and affordable to bulk customers without harm to providers of the services. It makes good sense. It's economic, efficient and promotes competition. Everybody benefits. Service providers benefit because operations and maintenance costs are reduced. They can shift or expand operations to more competitive markets and cover embedded costs and earn a return on facilities used by bulk shippers. Shippers benefit because they can make use of their equipment and realize lower transportation costs. Consumers should realize lower prices on products as providers' costs are reduced.

CONCLUSION

The ICC's regulatory policy is a striking mix of fanciful language and imaginative interpretation. It sets forth constraints that are wide open doors to naked monopoly power. It defines revenue adequacy so that no major railroad enjoys adequate revenue, or will, until there is ice in Hades. It defines competition so that it appears that only mule teams are not competition for railroads.

Ask yourself what regulator would change the accounting rules to inflate the so-called costs of service?

Ask yourself what regulator would then justify huge rate increases based on those inflated costs.

As yourself what regulator would set, as the maximum reasonable rate for a service, the cost to consumers of building the facilities to produce the service themselves.

The answer in each case is -- an ICC commissioner.

We are asking you to make national policy the reduction of energy costs by lowering domestic coal prices. The ICC needs to be restrained through amendments to the Staggers Act and the Sherman Act. Moreover, future vacancies on the ICC should be filled with individuals who are sensitive to America's energy needs and who are committed to conventional regulatory concepts and principles.

The resolution adopted by our Association and attached to my statement details specific items that the Congress should change in the Staggers Act that are in line with the Rahall-Ford Bill. These amendments are designed to clarify the intent of Congress by bringing fancy to firm ground and imagination to reality.

The resolution also espouses the substance of the DeConcini Bill which amends the Sherman Act. It attacks the problem of unchained railroad monopoly by providing for vigorous competition.

Mr. Chairman and members of the Subcommittee, ask yourselves why the sun is shining on the railroads on Wall Street, when we are told by the ICC that the railroads are out in the rain; ask yourselves, and answer for the citizens of America.

I urge your support: for the resolution, for the public interest and for the Nation's energy future.

Thank you.

Resolution Adopted By
the National Association of Regulatory Utility Commissioners

RESOLUTION

To Provide Reasonable Rates for Captive Railroad Traffic Under Standards Consistent With and Similar to Those Generally Applied by State Regulatory Commissions

AND

To Provide Shippers Access and Use of a Railroad's Facilities

WHEREAS, the Staggers Rail Act of 1980 provided for the deregulation of competitive rail traffic and directed the Interstate Commerce Commission to continue to maintain reasonable rates where there is an absence of effective competition for rail traffic within the Commission's jurisdiction; and

WHEREAS, over half of the electric energy in the United States is generated using coal, the majority of which is transported to electric utilities under non-competitive conditions by one railroad and subject to the jurisdiction of the Interstate Commerce Commission; and

WHEREAS, the Interstate Commerce Commission has issued a series of decisions effectively withdrawing regulation over the pricing of this captive rail traffic, including decisions which: (1) define "market dominance" so as to place ICC regulatory protection beyond the reach of many captive coal shippers; (2) set standards for "reasonable" rates which have no relation to the cost of providing service and which will allow coal transportation rates to double in real terms in five years; (3) exempt export coal from regulation although United States coal is already fifteen to twenty percent more costly than world market prices

due in large part to transportation costs; (4) define "revenue adequacy," on which several pricing freedoms for railroads under the Staggers Act are based, unrealistically, so that no Class I railroads, no matter how profitable, are considered to have adequate revenues, and highly profitable railroads will be allowed billions of dollars in extra rate increases; and

WHEREAS, customers of electric utilities will, unnecessarily, incur much higher electricity rates as a result of these ICC determinations;

WHEREAS, over the repeated objections of NARUC and individual state commissions, the Interstate Commerce Commission has usurped state authority to regulate intrastate railroad movements consistent with the Staggers Act; and

WHEREAS, the railroad industry, consumers and the captive shippers that serve them would benefit from (1) the restoration of competition to rail service areas now served by only one railroad and (2) the assurance that fair and reasonable freight rates are charged;

NOW, THEREFORE, BE IT RESOLVED that the National Association of Regulatory Utility Commissioners assembled at Washington, D.C. on March 1, 1984 urges Congress to enact legislation,

First to ensure reasonable rail rates for captive rail traffic, including provisions which:

1. Define "market dominance" in the context of effective competition for the transportation to which the rate applies, so that all captive shippers may obtain ICC regulatory review;

2. Require consideration, in determining "adequate revenues" for railroads, of several realistic indicators of financial health, and require:

   a. the use of embedded cost of debt,
   b. standard original cost depreciation accounting,
   c. other measures commonly applied by regulators in calculating the railroad's return on investment, and
   d. when appropriate, consider equity and debt costs to the holding company and look at the reasonableness of the transfer price between affiliates;

3. Require ICC consideration, in setting maximum reasonable rates, of the following standards:

a. the cost to the railroad of providing the service involved;

b. whether the traffic involved is paying an unreasonable share of the railroad's fixed costs;

c. the impact of the rate on national energy goals;

d. the extent to which railroad revenue shortfalls are attributable to hauling traffic at noncompensatory rate levels or failing to maximize earnings on competitive traffic; and

e. price stability and impact on shippers;

4. Require the ICC to calculate the inflation index (as set forth in the Interstate Commerce Act) upon which automatic rate increases are based on the basis of actual, not imputed, increases in costs; as well as allowances for productivity gains; and to require rail rates which have increased automatically with that inflation index to decrease when decreases in railroad costs lower that index;

5. Reauthorize and fund the Railroad Accounting Principles Board;

6. Require adoption of fair and reeasonable procedures for ICC review of state regulatory decisions on intrastate rail rates;

7. Prevent anticompetitive or predatory cancellations of joint rates;

8. Prohibit the Interstate Commerce Commission from exempting market dominant traffic from regulation; and

9. Prohibit the use of confidential pricing in shipping contracts, but in contrast make available all information necessary to ensure enforcement of (Long-Cannon) Congressional intent against cross subsidy; and

Second to require:

a. rail carriers to permit, with reasonable compensation, access and usage of facilities to shippers for whom the sole means of connecting with the trackage of another rail carrier or of reaching the destination of a shipment is over the railroad's facility; and

b. a review of line abandonment procedures to ensure against abandonment of rail service due to the operational preferences and/or strategic planning of the rail companies;

BE IT FURTHER RESOLVED that the National Association of Regulatory Utility Commissioners supports legislative initiatives to address these critical issues, and urges the Congress to enact legislation to obtain for captive rail shippers

1. protection from the practices outlined above, and
2. access to competitive rail service

and to obtain for consumers fair and reasonable regulation which protects them from exploitation.

Sponsored by the Subcommittee on the Staggers Act Implementation of the Committee on Electricity. Members include: Chairman Wesley H. Long, Public Service Commission of the District of Columbia; Ashley C. Brown, Ohio Public Utilities Commission; John B. Driscoll, Montana Public Service Commission; and Douglas P. Leary, North Carolina Utilities Commission.

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